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Business this week

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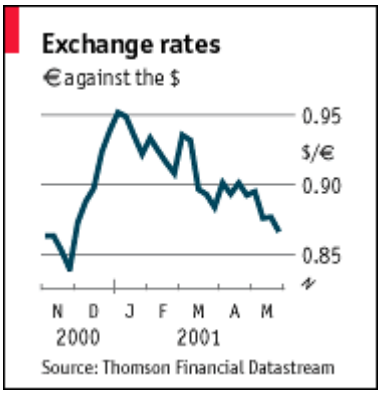
Growth slowed in the **euro-area's two biggest economies**. Germany's grew by 0.4% in the first quarter, and by 1.6% in the year to the end of March. French GDP grew by 0.5%, and by 2.7% over the year. Germany's consumer-price inflation jumped in May to 3.5%. The Ifo index of business confidence fell, suggesting that worse is to come. The poor outlook sent the euro to a six-month low against the dollar.

See article: Doubts about European economies



Britain's ups and downs

British Airways under Rod Eddington, chief executive for the past year, is on the up. The airline said that pre-tax profits had risen to £150m ($227m) last year compared with a low-flying £5m the year before. BA has cut costs and concentrated on more lucrative premium flyers.

See article: Mergers among European airlines are overdue

Marks and Spencer continued to founder under Luc Vandevelde, chief executive since the start of last year. Pre-tax profits at the struggling retailer fell from £417m to £145m, after exceptional charges. Mr Vandevelde's promised improvements have yet to materialise, although his self-imposed two-year time limit for them looms.

The **London Stock Exchange**, Europe's largest bourse, said it will float in July. That may be no substitute for the clear strategy it lacks. Continental rival Euronext hopes to beat the LSE to market.

See article: Stock exchanges are fast becoming publicly quoted companies

French connections

Vivendi, the world's second-largest media company, bought a former adversary, **MP3.com**, for $372m. In its quest to prevail in the provision of online music, the French company will deploy MP3.com's technology to distribute music through Duet, its alliance with Sony. Rivals Bertelsmann, AOL Time Warner and EMI have a similar deal with RealNetworks.

See article: France's growing enthusiasm for globalisation

Vivendi is also said to be talking to **Houghton Mifflin**, an American educational publisher, which it could acquire for around $1.7 billion. Vivendi is keen to add an American dimension to its European-based operations.

Lucent Technologies, the former telecoms-equipment arm of AT&T, reopened informal merger talks with France's **Alcatel**, which could create a firm worth some $77 billion. A deal may be hampered by Lucent's role as a supplier of highly secret communications gear to America's government; America may balk at a French company, in effect, taking over Lucent.

Rupert Murdoch's hopes of buying **Hughes's DirecTV** satellite-broadcasting arm may be upset by a last-minute bid for Hughes from **Echostar**, a rival satellite broadcaster.

Electricité de France, a European power giant, grabbed a 20% stake in Italy's Montedison to add to its pan-European holdings despite Italian government objections to it investing in the country's recently opened power market. France's government has been slow to open its own markets to foreign competition.

See article: France's growing enthusiasm for gloabalisation

Bank layoffs

Reuters

Goldman Sachs, a leader of the "bulge bracket" group of investment banks, is slimming down. It is likely to cut 12% of its staff, with proportionally more senior banking staff at risk than at other big investment banks that have announced similar cutbacks.

Citigroup decided that Salomon and Schroders no longer had a place in investment banking and will rebrand these units under its own name. Both old names were redolent of finance's history. Salomon Brothers, founded in 1910, epitomised Wall Street's free-wheeling cut-throat quest for profit in the 1980s. Schroders, founded in 1818, was for many years the essence of the staid, pinstriped world of the City of London.

MSCI, an American stockmarket-index group, announced details of a recalculation of its indices. The market capitalisation of companies has been adjusted to allow for a firm's "free float"—the availability of shares in the market. Investors will probably sell part-privatised state firms and those with extensive cross-shareholdings or large family stakes.

See article: Share indices reweighted

Latin temperament

AP

Facing energy shortages, **Brazil** announced plans for rationing electricity, aimed at achieving a 20% cut in consumption from July. The Central Bank raised interest rates after worries about the energy crisis had weakened the currency.

See article: Energy rationing in Brazil

Argentina received permission from the United States' Securities and Exchange Commission for a planned swap under which some $20 billion of its bonds expiring over the next three years would be exchanged for longer-dated bonds. The government hopes this will banish fears of a default, and speed recovery from an economic slump.

Keep your hair on

Procter & Gamble's management may have sprouted grey hairs implementing a corporate restructuring but it has tried to solve the problem with the acquisition of Clairol, a hair-dye and shampoo firm, for $4.9 billion, from Bristol-Myers Squibb.

See article: Procter & Gamble's purchase of Clairol takes it into a fast-growing market

Ford said that, as a precaution, it would recall a further 13m Firestone tyres fitted to its vehicles at a cost of some $3 billion. It recalled 6.5m tyres last year that were linked to 174 deaths and many more injuries. Bridgestone, Firestone's Japanese parent company, severed a 100-year relationship with Ford, partly blaming it for the problems.

See article: The second recall of Firestone tyres by Ford

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Politics this week

May 24th 2001
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Glimmers of change

AP

Israel's prime minister, Ariel Sharon, welcoming the **Mitchell report**'s call for a ceasefire, said that Israeli soldiers would fire only when in direct danger. But the Palestinians demanded the complete acceptance of the report, including its call for a freeze on Jewish settlements. Not surprisingly, the violence continued. Colin Powell, America's secretary of state, cautiously entered the scene, appointing a diplomat, William Burns, to be America's new man in the Middle East.

See article: Ceasefires and settlers in the Middle East

George Bush had a hard week in the Senate. Senator James Jeffords of Vermont announced his resignation from the Republican Party, leaving the Democrats in control of the Senate. The Senate approved the country's biggest tax cut for 20 years, reducing the tax burden by $1.35 trillion over the next 11 years.

See article: Jim Jeffords's defection

Argument raged in the **European Union** over the distribution of its regional aid once poorer Central and East European countries join. After Spain, Italy's likely new finance minister urged no undue haste to enlarge the Union: Italy had to think of its own south first.

See article: An EU row over regional funds

War and peace

India ended its six-month-old ceasefire in **Kashmir**, saying that militant groups had continued their campaign of violence. It invited Pakistan's military ruler, General Pervez Musharraf, to Delhi to discuss Kashmir's future.

See article: Kashmir

A landmine planted by Sri Lanka's **Tamil Tiger** guerrillas blew up a bus carrying sailors, killing 17.

America's secretary of state, Colin Powell, set off to visit Mali, South Africa, Kenya and Uganda, to discuss economic, political and health issues. Meanwhile, a team of ambassadors to the UN toured **central Africa** in search of peace. One of the rebel Congolese groups offered to withdraw from frontline positions in exchange for humanitarian aid.

Colombia's Congress killed a proposed reform that would have changed the electoral system. President Andres Pastrana had hoped the reform would encourage the country's guerrillas to make peace.

See article: Setbacks for reform in Colombia

China cross

EPA

Visits by the **Dalai Lama** and **Chen Shui-bian**, the president of Taiwan, to the

White House prompted China to protest that the United States was interfering in its domestic affairs.

The **Siberian cities** of Irkutsk and Ilensk were hit by floods from the ice-blocked Lena river. Russian air-force planes bombed the blockage.

Criminal elements

An Egyptian court sentenced **Saadedin Ibrahim**, a well-connected sociology professor, to seven years' imprisonment. He was accused, among other crimes, of defaming Egypt's reputation.

See article: Egyptian security

In a rare attempt to curb their activities, 26 "war veterans" were arrested in **Zimbabwe** and charged with trying to extort money from private businesses. Disillusioned, some of them said they would join the opposition.

The estimated 1,700 Hindus and Sikhs in **Afghanistan** were ordered by the ruling Taliban to identify themselves by wearing yellow badges. The Taliban claimed that the badges would protect non-Muslims from the attention of the religious police.

See article: The Taliban turn on Hindus

Just not cricket

In **Britain's election** campaign, the Conservative Party was split wide over the EU. Leon Brittan, a former EU commissioner, blasted his party leadership's "visceral hostility". Margaret Thatcher said, were she in office, she would "never" give up the pound for the sovereignty-sapping euro.

Reuters

See article: The paradox of Conservative euro-policy

An investigation by a former senior British policeman into corruption in **cricket** found that it had started in England and spread worldwide. It now involved allegations of murder, kidnapping and drugs.

Germany calling

A leaked cable from **Germany**'s ambassador to Washington revealed that Chancellor Gerhard Schröder had urged George Bush to ensure that Russia got no more aid unless it blocked capital outflows. President Vladimir Putin was not pleased.

See article: German diplomacy of a sort

A scheme for **German** business to compensate former slave labourers of the Nazis looked ready to go ahead—at last—after a court in New York had dismissed claims brought there.

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America and the Middle East

No exit?

May 24th 2001
From The Economist print edition

America must help Israel and the Palestinians to find one

Get article background

AFTER Bill Clinton's tribulations, any sensible American president would have done his damnedest to avoid being drawn into the Middle East's most intractable conflict. George Bush made it clear from the start that he would not be involved in the soul-destroying intricacies of helping Jews and Arabs to find a way of living together, but would be casting his regional eye farther east, reviewing policy towards two other difficult people, the Iraqis and the Iranians (see article). But the issues are linked: the Israeli-Palestinian conflict is an unfolding tragedy that could have a decisive effect on America's other interests in the region. So Mr Bush, however reluctantly, is allowing his secretary of state, Colin Powell, to become tentatively involved, and William Burns, America's ex-ambassador to Jordan, has been named special assistant on the Middle East. A beginning, but that is all.

The job to be done now is nothing like the one that led Mr Clinton and his team to spend endless days and nights trying to get the Israelis and Palestinians to agree to a lasting settlement. Neither side is ready for another attempt at that, and when they are they may be best left to their own devices. The urgency now is to stop the killing.

Without American intervention, the ever-escalating cycle of violence in the West Bank, Gaza and Israel is unlikely to wear itself out. Israel is now run by a prime minister, Ariel Sharon, who believes that the way to bring the Palestinians to heel is to crush them. He and his generals have considerable crushing means at their disposal, from fighter-bombers to tanks, and he has promised his people that, by using military might, he will make their lives more secure. The Palestinians, having thrown away the chance of a half-decent settlement when Israel was under Ehud Barak, are resisting being crushed in the only way they now see open to them. Though puny by comparison, they are demonstrating to the Israelis who occupy their country that, contrary to Mr Sharon's pledge, his policy makes the occupiers' lives more perilous, not more secure. Both sides, in their separate ways, are capable of inflicting great pain on the other. In all probability, neither can win.

The spreading disgust

Can they be left to get on with it, with the United States blowing a wordless curse in the direction of both houses? Mr Bush might prefer that, but it really will not do, and not only for humanitarian reasons. The conflict, as it rages on, is spreading its virulence, beginning to infect Arab governments that are important to America's self-interest, both for strategic and energy reasons. In Arab and other Muslim eyes, the United States is already deeply embroiled in the region's problems through its unwavering support for Israel: the $3 billion of America's money that goes there each year, the faithful backing in the UN Security Council, the acquiescence with most Israeli policies. The Arabs' belief that America is unbalanced in its attitude towards Israel is already hampering other policies in the area. It makes it harder, for instance, to persuade Iraq's neighbours to stop Saddam Hussein's smuggling, and it frustrates attempts to put American-Iranian relations on a less hostile footing.

This is not to suggest cracking the bond between America and Israel. That bond must and will endure, if only because Israel remains a democracy, in contrast to almost all the other countries in the region, and the Palestinian Authority too. But friendship does not, and should not, exclude honest criticism—more

perhaps than Mr Clinton was ever prepared to offer: he never asked Israel to do more than its prime minister, Mr Barak, was prepared to do. In fact, the Bush administration may not care much for Mr Sharon, or what he is now doing. But bland, general appeals for an end to the violence will neither bring that violence to an end nor help restore America's reputation in the Middle East.

Stop those settlements

For the violence to end, both Mr Sharon and Yasser Arafat need to show their people that they have gained something from the pain the conflict has caused them. A formula to help them to this point is ready and waiting in the Mitchell report, the recommendations of an international committee headed by George Mitchell, a former American senator. The report provides a blueprint. Israel's gain would be an end to the Palestinians' guerrilla war and terrorism; the Palestinians' gain would be a halt to Israel's expansion of Jewish settlements in the West Bank and Gaza. The Palestinians, endorsing the report in its entirety, have called for a summit to talk about ways of carrying out its recommendations. But Mr Sharon, while echoing the call for an immediate ceasefire, has turned down the report's crucial confidence-building demand for a freeze on all settlement construction, including expansion for what the Israelis disingenuously call "natural growth".

Mr Sharon has to be encouraged to change his mind, and the encouragement has to be delivered, in unmistakably blunt words, by the Americans. Mr Powell, while endorsing the report, seems to go along with Israel's reservations by fudging the call for a settlement freeze. That will not do the trick.

Israel, confident in having the world's only superpower as its loyal ally, does not much care what others are thinking: it was brusque this week in its rejection of unusually sharp criticism from the European Union. But, earlier this year, a word from the Americans caused Mr Sharon to make Israel's tanks do a sharp U-turn out of the Palestinian-controlled territory they had invaded. Establishing Jewish settlements is even closer to Mr Sharon's heart than military adventure, but the settlements negate all chance of Palestinian-Israeli peaceful coexistence, and understandably so: which self-respecting people would allow their land to be thus expropriated?

Accepting the Mitchell report in its entirety would mean an end to the current round of violence. Admittedly, that is all. Almost certainly, the stop would be just temporary. The whole miserable business might well start again; a lasting peace settlement remains buried beyond the horizon. Never mind: stopping the slaughter is worth doing for its own sake. The killing is leading to nothing good. It is a tragedy in itself.

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Control of the Senate

Post-Jeffords

May 24th 2001
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George Bush will have to change tactics—a little

AP

AFTER Enobarbus defected to Octavius, Antony sent his old friend all his treasure; overcome with remorse, Enobarbus killed himself. Something of the kind might now work well for George Bush in dealing with Jim Jeffords, the Republican senator who this week left his party, handing control of the Senate to the Democrats and dealing a body blow to Mr Bush's legislative ambitions. The idea would not be to kill the traitor, you understand, but merely for Mr Bush to recover, through a gift of compromise, what he can of his plans.

Certainly, those plans are now impaired. Mr Bush should still get a big tax cut through Congress. But his education proposals are likely to be watered down even further. Conservative causes, such as packing the judiciary with right-wingers, look like non-starters. The Clinton administration picked up steam after a disastrous first hundred days. Mr Bush's best days may already be behind him.

Does the Jeffords defection show that Mr Bush made a tactical mistake? So far, the president has ignored the closeness of his election. Having run as a conservative, he unveiled a conservative programme and set about implementing it with remarkable efficiency. Granted, he was pushing his luck: Mr Jeffords shows that. Still, it is hard to imagine that he would have got so far so quickly if he had yielded from the start.

In any event, the question is, what now? The best course is to make a virtue of necessity. The president's initial bout of conservatism has shored up his base; looking forward, it makes political sense to move a step to the centre, to woo the moderate voters the Republicans will need next year to recapture the Senate. So far, Mr Bush's efforts at bipartisanship have concentrated on finding individual Democrats to back particular measures (he persuaded eight senators to support his tax plan). Now he will have to deal with the Democratic leadership—and above all with the new Senate majority leader, Tom Daschle—more directly.

In Mr Bush's favour, he still has momentum, and, unlike his father, he has his party's right wing under control. The trick will be choosing where to spend his diminished political capital. Fighting for, say, more oil drilling in Alaska might be to squander his resources. Battling for Social-Security reform—something that most Democrats realise has to happen sooner or later—looks more worthwhile. Two especially promising areas might be campaign-finance reform (something he has treated rather snootily so far) and Medicare reform (where Congress nearly produced a deal under Mr Clinton).

The president has already compromised on his tax-cut bill and even on his energy plan. When he was governor of Texas, he worked well with his opponents. On the campaign trail, he moved between friendly talk about changing the tone in Washington and bouts of petty vindictiveness. He should avoid the latter—and punish Mr Jeffords with compassion.

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Liberalising aviation

Unfinished business

May 24th 2001
From The Economist print edition

Only Brussels can open Europe's wider skies

Get article background

THE freeing of Europe's aviation business from government interference over the past four years justifies a certain measure of satisfaction. National flag carriers no longer put their hands out for state subsidy: most have been privatised or are about to be. Competition between European airlines has increased. And new, low-fare start-ups are raising their share of the market (see article). So good news all round?

Not quite, as the European Commission understands only too well. It is taking legal action against eight of the ten EU governments that have signed "open-skies" agreements with the United States. The commission's legalistic point is that aviation deals with non-member countries are, as trade agreements, properly the competence of Brussels. Yet national governments have, for narrow, protectionist reasons, repeatedly failed to let the commission exercise its external-trade mandate in aviation, even though it has liberalised the internal European market.

This may sound like another argument about "subsidiarity", the notion of devolving powers inside Europe to the level of government that is best-fitted to exercise them. And so it is, in a way. But constitutional doctrine is not the only thing that is at stake. Bilateral open-skies deals have meant real progress in the glacier-like process of opening international aviation to real competition. Yet they suffer from big drawbacks, which could now act as a brake on further competition. The main objection is not the popular one that they have favoured American airlines unduly by letting them roam around the internal European market while not allowing the Europeans to do the same in America—although they have. The bigger point is that they are delivering a false "liberalisation" that raises rather than lowers barriers to entry.

The open-skies deals that the Americans have struck with the Germans, Dutch, French and others lift all controls over who flies where, when and at what prices between any destinations in the countries at either end of transatlantic routes. That sounds as if it should unleash competition that might even reduce the notoriously high fares paid by business travellers to cross the Atlantic. But this is a sham. For the open-skies deals have gone hand-in-hand with antitrust immunity given to designated national flag-carriers, which have entered into alliances with their chosen partners across the pond.

Thus the antitrust immunity in the German-American open-skies deal has allowed United Airlines and Lufthansa to pool some of their services across the Atlantic. This means they can conspire to reduce capacity and raise fares—all, ironically, in the name of free trade. In practice, the only real competition to Lufthansa and United in Frankfurt, or to Air France and Delta (another alliance, blessed by the Franco-American deal) in Paris, could come from a non-German or non-French carrier, with the infrastructure and financial muscle needed to run competing services. Only when British Airways, say, is free to compete across the Atlantic from Paris, Frankfurt or Amsterdam, with its continental competitors doing the same from London, will that happen.

Free trade in the air

The European transport commissioner, Loyola de Palacio, has proposed the idea of a transatlantic common aviation area, which is now supported by many Americans who see it as a way to open London Heathrow to more than two favoured American carriers. But BA will support the opening-up of Heathrow

only if it wins the same antitrust immunity for its plans to collude with American Airlines that its European competitors have won with their chosen partners. The British government is against handing negotiating power to Brussels, just as other European governments are, mainly because they want to protect the cosy deals that their flag carriers have with their American counterparts. Only if Brussels speaks for all Europe is there a chance that both the European and American markets will be truly liberalised.

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Stockmarkets

Floating in the air

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Stock exchanges should be public companies, and clearing agencies should be utilities

IT SOUNDS positively incestuous. But the fashion for stock exchanges to turn themselves into companies that are listed and traded in their own marketplaces, first started some years ago by Sweden's exchange, has now become all the rage. This week Norway's stock exchange completed its float, and the London exchange confirmed plans to go public later in the year. Deutsche Börse went public in February. Euronext, the alliance of the Paris, Amsterdam and Brussels exchanges, will shortly launch its own initial public offering (IPO).

The action is not confined to Europe. America's Nasdaq stockmarket is preparing to float itself as a public company. Last week Instinet, an electronic broker-dealer formerly owned by Reuters that is seeking regulatory approval as an authorised exchange, launched its own IPO. Even the Tokyo Stock Exchange is considering demutualising and floating. Soon the only hold-out may be the biggest of them all: the New York Stock Exchange. The NYSE's chairman, Dick Grasso, had hoped to demutualise and go for a public listing, but he was overruled by his powerful specialist member firms. The same members also insist on keeping the NYSE's expensive and anachronistic trading floor, when almost all the rest of the world's exchanges have gone electronic.

There are strong arguments in favour of exchanges turning into public companies. As they compete increasingly with electronic rivals (and with each other), they have become, in essence, little more than rival platforms for trading securities. The old notion of a national stock exchange as a natural monopoly-cum-utility has become not just antiquated but actively harmful. It has been used to justify delegating regulatory functions, such as listing rules or policing insider trading, to exchanges, when these would be better handled by disinterested external regulators. Moreover, rather than being clubs that respond only to their members' vested interests, publicly traded exchanges have to satisfy the needs of their real customers: companies and investors. It may also be easier to arrange mergers of publicly traded exchanges, especially in Europe, which is saddled with too many bourses.

A clearer utility

There is, however, one downside to the process of turning Europe's stock exchanges into fiercely competing companies. It may make it harder to rationalise the continent's multifarious clearing and settlement agencies. Some of the exchanges, including Deutsche Börse and Euronext, own their own clearing and settlement arms, either wholly or in part. Yet, thanks to economies of scope and scale, the business of clearing and settlement genuinely has a large element of natural monopoly about it. As European cross-border share trading grows, so will demand for a single clearing and settlement agency, rather along the lines of America's Depository Trust and Clearing Corporation. The cost of clearing and settling a cross-border securities trade in Europe is ten times as high as it is for an equivalent trade in America.

The solution is not to discourage Europe's exchanges from becoming companies, but to encourage them to divest their clearing and settlement arms. The way would then be open for market participants to push these arms into a single utility, or perhaps two or three interconnected utilities. Not for the first time, Europe has had things backwards. Stock exchanges, long seen as public utilities, should be competing companies; but clearing and settlement agencies, many of which are now companies, ought to be considered more as utilities.

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Afghanistan

The monster

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From The Economist print edition

It's high time their Islamic friends reined in the Taliban

AP

IN JANUARY, the supreme leader of the Taliban, the self-styled Islamic students who rule Afghanistan, declared that anyone converting to Christianity would be executed. In March, the Taliban proudly set about the destruction of two enormous Buddhas that dated back to between the second and fifth centuries AD. Now comes the announcement that all Hindus in Afghanistan will have to wear a badge or label to distinguish them from Muslims. Soon there will be no more religions for the Taliban to insult.

The insults, however, will matter less than the injuries, if those are what follow next. History elsewhere suggests they may. The Nazis were not content with an edict that all Jews should wear the Star of David. The government in pre-genocide Rwanda was not content with symbols in documents indicating that the bearer was either a Hutu or a Tutsi. Since the Taliban have never been shy of violent punishment of even co-religionists deemed guilty of offending Islam, it would be foolish to imagine that the followers of other religions are safe.

Nor are neighbouring countries. Islamic zealots, trained in Afghanistan, are now the terror of the governments of Kirgizstan, Tajikistan and Uzbekistan. Though it may suit the authoritarians who run these ex-communist countries to make much of the threat to their regimes, a threat of some kind undoubtedly exists. The Taliban also have a symbiotic relationship with Pakistan, which appears at once to fear and to sustain the regime next door.

Farther afield, the Taliban are accused of helping Islamic rebels in Chechnya, to the fury of Russia, and in Kashmir, to the fury of India. China dislikes them. The United States—though it nourished them when they were fighting the Soviet Union—hates them: they shelter Osama bin Laden, the Americans' most wanted terrorist, blamed for masterminding the blowing up of two of their embassies in Africa in 1988 and bombing the *USS Cole* in Yemen last October. Only Pakistan, Saudi Arabia and the United Arab Emirates recognise their regime.

No wonder then that the United Nations, at America's behest, has imposed new sanctions on Afghanistan. That, however, merely increases the isolation of the regime—it led this week to the departure of all the UN's political staff—and intensifies the suffering of the hundreds of thousands of Afghans already driven from their homes by drought, disruption and years of civil war. All the signs suggest that, with the arrival of summer, that war is about to be renewed.

The Taliban's few friends, stout Muslims all, have a duty to use their influence to end the many practices in Afghanistan that bring Islam into disrepute. And Pakistan, whose support is crucial to the regime, has a particular duty. It fears being devoured by the monster it feeds. But appeasing that monster will do the Pakistanis no good in the long run—and add to the suffering of many Afghan innocents in the meantime.

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The European Union's enlargement

A matter of priorities

May 24th 2001
From The Economist print edition

If it comes to a choice, the EU should put expansion before spending reform

Get article background

THE leaders of the European Union like nothing better than giving lofty speeches about "solidarity", "unity" and the "historic obligation" to admit new members from the east. But lock the same leaders in a room together and the high-falutin talk quickly gives way to something rather more basic: a raw struggle for power and money, especially money.

That is now on full display. The commitment to admit the ex-communist countries to the east is being qualified by a series of increasingly blatant attempts to rig the rules against the newcomers. If this new round of haggling gets out of hand, the EU's next expansion, first promised in 1990, could be indefinitely delayed, or the applicants could be presented with a deal so unattractive that some will reject it. Opinion polls in Estonia, one of the front-runners for early membership, already show a majority of the voters opposed to joining the EU.

The root of the problem is easily stated. The applicants are poor, and they are many. Expanding the EU to 27 members by admitting all who want to join, except Turkey, would increase the Union's population by almost 30%, but its GDP by just 5%. This matters because the EU transfers money from one country to another. Its overall budget amounts to over 1% of its members' combined GDP—and about 80% of this total is accounted for by regional aid and by the common agricultural policy (CAP), which are respectively intended to subsidise poor people and farmers. As luck would have it, Central and Eastern Europe is full of poor people and farmers.

It was always plain that enlargement would involve some painful political decisions. Three in particular, raised by Germany, Spain and France, are proving awkward.

The German problem is a fear that, given the huge income disparities between Germany and the countries to its east, their membership of the EU will bring an uncontrollable influx of job-seekers. So Germany has extracted from the European Commission a seven-year restriction on the free movement of labour. Now that Germany has a concession, France and Spain are piling in. Spain is the largest beneficiary of the programmes that give help to the EU's poorest regions, and the Spanish know that, once the easterners join the Union, most of their regions will no longer qualify for aid under the EU's rules (see article). So they want the rules rewritten, to ensure that the subsidies keep flowing. They are getting increasing support from Italy, Portugal and Greece.

France has a similar concern to the Spanish one. It is by far the biggest recipient of EU agricultural subsidies. But if Poland joins the Union, it will bring with it regiments of farmers, all wanting an equal share. That will either mean less for France, or a big increase in the EU budget. The preferred French solution is clear: find an excuse to deny the applicants full access to the farm programme.

The best, the enemy and the good

It is not hard to sketch out an ideal solution to these difficulties. If enlargement makes both the CAP and regional aid financially unsustainable, why not seize the opportunity to abolish or drastically scale back both programmes? It is far from clear that regional aid has been effective: think of all the money poured into Italy's Mezzogiorno over the years to the benefit of almost nobody but the Mafia. As for the CAP, it is

widely acknowledged to be a wasteful tax on consumers. Talks about liberalising farm trade, coupled with new enthusiasm for greenery and public anger at the spread of mad-cow disease in Europe, are adding to the pressure for reform.

It would be nice to think that the prospect of enlargement could be used to force the existing 15 to reform both the CAP and the regional funds in advance, but that could be a trap. It risks playing into the hands of those who would like to delay the EU's expansion indefinitely, ideally keeping the CAP as little changed as possible. If the EU has at some point to choose which should take priority, spending reform or enlargement, the answer should be clear: enlargement first.

But how can the EU expand without nailing down the budgetary implications? Easily, as it happens. The financial framework for the budget runs out in 2006. As things stand, the first new members are unlikely to get in before 2005. There would be enough money in that year to pay for the first newcomers. Once in, they could help make the rules, rather than having to accept a *fait accompli* rigged against them. A messy fight would ensue, but that would be better than forfeiting enlargement.

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The test-ban treaty

In America's interests

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Why George Bush should embrace a nuclear-test ban

Corbis

NOT even the world's most powerful country can know everything. America's intelligence officials have been fretting over strange goings on at China's nuclear-test site at Lop Nor in Xinjiang province. Is China conducting "zero-yield" nuclear experiments, as America does from time to time? These produce no nuclear chain reaction and are allowed by the Comprehensive Test-Ban Treaty, which both countries have signed (though not ratified). Or is China breaking the ban, as some claim, conducting explosive tests so small that even America's sensitive ears cannot pick them up? It is vital to know, at a time when all the nuclear powers, whether they have signed the treaty or not, say they have forsworn testing.

To test-ban critics, continuing doubts about the activities of China and also Russia—at its Novaya Zemlya test site in the Arctic—show that a test ban is inherently unworkable because the ban cannot be adequately verified. That is one reason, says President George Bush, why he will not resubmit the treaty for ratification by the Senate, which rejected it in 1999 in a bitterly partisan vote. But the Lop Nor goings-on show instead why Mr Bush is wrong not to back a treaty that is probably more in America's security interests than anyone else's.

Monitoring is crucial to a test ban. That is why the international system being set up to support the treaty not only encourages openness, but assumes someone may indeed try to cheat. Its still expanding networks of sensors—on land, under the oceans and in the atmosphere—is already far more extensive, and sensitive, than anything America can mount on its own. Such coverage is essential to deter cheats if possible and to detect them if necessary, since below five kilotonnes of explosive yield it becomes hard to tell a nuclear test from an earthquake, and below one kilotonne a test might be taken for a large chemical explosion. And if doubts linger? The treaty provides for on-site inspection if it seems something fishy is going on—a right worth having at Lop Nor just now.

Mr Bush, however, has a second worry: that without explosive testing, America's nuclear weapons will become less safe and effective. Allowing that to happen would indeed be folly. Nuclear weapons cannot be disinvented, though they can be reduced greatly in number, as Mr Bush himself proposes. So the robustness and reliability of America's nuclear deterrent remain crucial to security and stability: America and its allies need to be confident that the weapons that remain will go bang if needed, and only if needed.

Yet America has long been better rehearsed than anyone in doing this, using the computer modelling, non-explosive testing and other work allowed by the treaty. That is why it has not needed to test since 1992. Many of its nuclear scientists would argue that to keep up these non-testing skills requires more money. But unlike verification, which is best done in treaty co-operation with others, the remedy here is entirely in Mr Bush's hands. And if America's weaponeers did encounter some unfixable problem that put its nuclear deterrent in jeopardy? It has the right to pull out of the treaty.

The test-ban treaty will not disarm America. Nor will it stop someone building a crude fission bomb, untested. But it will slow the proliferation of more complex weapon designs that do need testing—by a newcomer wanting to build a more powerful thermonuclear bomb, or a China, say, wanting to mount multiple warheads on mobile missiles, or a hostile power hoping to use small nuclear weapons to offset America's huge advantage in conventional forces.

Fashion victim

America has the safest, most sophisticated nuclear arsenal in the world. A test ban will help, verifiably, keep it that way. Mr Bush has singled out proliferation of weapons of mass destruction as the greatest threat America faces. The test-ban treaty would better track the proliferation habits of others. International treaties are not the vogue in Mr Bush's Washington, but he rejects this one at America's peril.

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Letters

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Rich man, poor man

SIR – On Robert Wade's powerful piece about the increase in global inequality (By invitation, April 28th) you say that "without longer runs of data it is hard to know whether this change is part of a well-established trend...or a short-term fluctuation" (Economics focus, April 28th). In "Monitoring the World Economy 1820-1992" (OECD, 1995), Angus Maddison tracked the widening global gaps and showed that the gap in constant purchasing-power prices between the poorest and the richest countries rose from just over three to one in 1820 to over 70 to one in 1990. Though some global gaps have narrowed, at least in relative terms, the income gaps between the richest and the poorest people and countries have not.

The widening gap between the developed and the developing countries was called "the central problem of our times" by the Pearson Commission three decades ago. Since then the gap between the richest and the poorest has more than doubled.

Sir Richard Jolly
University of Sussex
Brighton

SIR – The evidence does not support Mr Wade's assertions that the global distribution of income is becoming "ever more unequal" and that the trend is "worsening rapidly". On the contrary, most studies suggest that the past 25 years have seen a reversal in the trend towards widening inequalities which had been proceeding for two centuries.

Mr Wade's confidence that he has drawn upon "probably the most reliable dataset on world income distribution" is absurdly misplaced. His analysis relies on household surveys alone. Far from a virtue, this is a massive deficiency. One effect is that such important elements of national product as public spending on goods and services have been left entirely out of account. The relative size of these components differs greatly between countries and over time, and can be particularly important in the level and growth of real living standards in the poorest countries. This key problem illustrates the importance of using concepts of income that are germane to the purpose of the discussion.

Ian Castles
Vice-president, Academy of the Social Sciences in Australia
Canberra

SIR – Mr Wade is right to note the relative neglect of the inequality issue in international institutions and in the treatment of developing countries in mainstream economics. But both his contribution and your rejoinder are stuck in the framework of a well-worn debate about the merits of open markets and globalisation. Mr Wade set the bait by asserting (on the basis of no good evidence) that global inequality is rising because of liberalisation and globalisation. You bit, pointing out that no amount of hand-wringing about inequality can undo a simple fact—that the real losers in today's global economy live in Africa, rural India and other places that globalisation has bypassed.

You both miss the two real challenges that global inequality poses. First, whether rising or not, because of globalisation or not, global inequality is shockingly high. We are so rich in the advanced economies that small transfers to poor countries could transform the lives of our fellow global citizens. I doubt that fear of social disruption, as Mr Wade seems to hope, will move the rich world to action. Leadership and appeals to humanity are likely to work better, as the public pressure for debt relief and affordable medicines in Africa has shown.

Second, inequality within countries, particularly developing countries where markets are shallow and governance is poor, is probably itself contributing to low growth. In Brazil, Mexico, Thailand and South Africa, the poorest 40% of households produce and control as little as 5% of their countries' resources. In these and other developing countries with weak capital markets, underfunded public schooling, and inadequate judicial systems and contract enforcement, the poor are likely to be elbowed out of access to jobs, credit, and other opportunities to be productive. If half of the population is locked into low-productivity work, overall growth will obviously be limited. Moreover, a high concentration of income at the top encourages and sustains the corruption and incompetence that in the worst cases add up to kleptocratic states. It also encourages a resort by politicians to populism and protectionism, undermining the open markets and democracy that ultimately are the keys to reducing both poverty and inequality.

If inequality contributes to low growth, and low growth sustains high poverty, then an attack on poverty requires an attack on the problem of inequality. Next time I hope *The Economist* will move beyond the growth debate to underline this point.

Nancy Birdsall
Carnegie Endowment for International Peace
Washington, DC

SIR – Mr Wade has argued that reducing international inequality should be an overarching priority. You reply that a "strange implication"of his position is that a country with a more egalitarian distribution could be regarded as a greater success even if it has more people in absolute poverty. There is an obvious resolution of this dilemma: to regard economic wellbeing as depending on both inequality and poverty. What Mr Wade, *The Economist* and the rest of us all seek is a world in which both inequality and poverty are falling. But inequality is rising as poverty is falling. Are things getting better or worse? Reasonable people can and do disagree.

Gary Fields
Cornell University
Ithaca, New York

Lowering the flag

SIR – How can Doug Schaden (Letters, May 12th) write with any integrity, from California of all places, that the "Union Jack" (more properly the Union flag—the Union Jack is only hoisted at sea) is a symbol of imperialism and oppression.

The American flag is habitually burnt publicly around the world by anti-imperialists while the Union flag rarely is, if ever. Second, the Stars and Stripes flies over the states of California and Texas, which America took by force from Mexico fewer than 150 years ago (that is why Mr Schaden's town, Santa Rosa, has a Spanish name). Mexicans still call these states the occupied territories. Unlike Britain, America has not yet decolonised, and continues to act in a brutal, imperialist fashion in many parts of the world. But what can one expect from a nation whose creation involved the genocide of one race and the subjugation of another?

David Short
Johannesburg

Death sentences

SIR – It does not require "absolutist" thinking to oppose the death penalty in all instances ("The rights and wrongs", May 12th). It simply requires a clear-minded recognition that the death penalty's brutalising futility achieves nothing but more violence. Recent figures compiled by Amnesty International show that not only is America's pro-death penalty stance supported by a dwindling band of nations, but also that only China and Saudi Arabia officially killed more prisoners than the United States in 2000.

Add the fact that America is now a world leader when it comes to executing juvenile offenders and it becomes clear that this is a country divorced from mainstream world opinion on the issue. Execution is not, as you contend, the "strongest statement you can make"; it is the ultimate expression of judicial despair.

Richard Bunting

Communications director, Amnesty International UK
London

SIR – You argue that Timothy McVeigh wants to become a martyr and do yet more damage from beyond the grave. Thus we should let him live, giving him no opportunity to make grandiose proclamations or quote more bad poetry before making a histrionic exit.

This is wrong on two counts. First, it distorts the jurisprudential aspects of the case. The severity of the crime should be the sole consideration in setting the sentence; guesswork about how to moderate the activities of presumed extremist groups is not admissible. Second, Mr McVeigh will never be an inflammatory symbol for any movement. People wearing McVeigh T-shirts will probably get beaten up in bars.

Lawrence Barnes
Bangkok

SIR – Stop wasting newsprint and readers' time with tedious examinations of America's death penalty. No one on this side of the Atlantic cares or even notes what Europeans think about the death penalty, and with good reason. A continent which spawned two world wars and a cold war in the 20th century and which had to be rescued repeatedly by America has no moral lessons—none—to impart to us.

Richard Sybert
Thousand Oaks, California

Electoral race

SIR – Surely, if Cheltenham (which the Conservatives lost, with a black candidate, to the Liberal Democrats in 1992) was as you say "a safe Conservative seat when the candidate is white" ("Plagued by race", May 5th), the Conservatives should have won the seat back at the next election, when their candidate was white. Instead, the Liberal Democrats held on to the seat with an increased majority.

In fact, it was not a safe Conservative seat. The Conservative majority at the 1987 general election was 4,896, which qualified it as a marginal. The swing against the Conservatives to the Liberal Democrats in Cheltenham in 1992 was 5.2%. At that election, the Conservatives suffered larger swings against them in many other constituencies, particularly in the south-west of England. The Liberal Democrats had been targeting Cheltenham, and were thought likely to win it before the Conservatives selected John Taylor as their candidate.

Alex Macfie
Oxford

Colombia's drug problem

SIR – Your survey stops short of suggesting the only way out of Colombia's predicament (April 21st). It is possible that after many more deaths and many more billions of dollars spent on weapons that Colombia regains a peace of sorts, but only because the drug business has relocated. The developed world should realise that the War on Drugs is lost on the home front and the time for legalisation has arrived.

Bernardo Recaman
Bogota

SIR – I would like to add two comments to your survey of Colombia. First, the degree of openness in Colombia's democracy is much higher than we Colombians are willing to recognise, or the world to understand.

Second, you should not use the word paramilitary. The AUC was not created, armed or trained by the military, nor does it receive logistical support from them—the proper definition of a paramilitary force. It is necessary to understand this distinction in order to solve the issue of the AUC.

Some believe that the army actively supports paramilitary groups and so government policy must be directed to punishing the army for supporting the AUC. Others recognise that the AUC is independent of the army, and that government policy must be directed to make the army persecute the AUC as

criminals. The Colombian government has taken the second approach. Unfortunately, most European governments see the army as part of the problem. Thus support for Plan Colombia is meagre because of this incorrect view.

Alfredo Rodriguez
Bogota

SIR – You give a misleading impression by saying that in the past the two main political parties "became perhaps the only truly national institutions". There is another that began operations in 1500 and to which the majority of Colombians belong. Like all old and inherently bureaucratic institutions it has many faults but its leaders condemn unhesitatingly and fearlessly the hard men on all sides of the conflict: many of its members pay for their work with their lives. No one could deny that it is one of the main elements of stability in our society. Although I do not belong to the institution, I am surprised that you did not mention the Catholic church.

Fred Tiffin
Cali

Basle's bank rules

SIR – Europe certainly would be "wrong to try to apply new international rules on bank capital in a uniform way" ("Don't bank on Brussels", April 21st) but no one is advocating that they should. It is misleading to say that the EU proposes to apply the same rules to investment firms and small savings banks as to large, internationally active "Basle banks". The EU proposals set out a structured approach designed to enable banks with differing levels of sophistication to use different systems. Nor is there any proposal to subject investment firms to the same range of charges for different risks as, in most cases, operational risk is the only one that such firms actually bear.

The proposed new charge for operational risk does cause very serious concern, however, and can indeed be described as "raw and untested". The key problem is calibration. The charge is simply too high, and the simpler options for calculation, such as a percentage of income or assets under management, bear no relation to risk actually incurred. If the problems with operational risk are resolved there is no reason to believe that the cost of lending by small banks to small businesses will increase.

Although significant problems remain with the latest draft of the new Basle Accord, you are wrong to write off the proposals in their entirety. A lot more work needs to be done but the problems can and should be resolved. Fracturing the globally agreed framework would be a setback for systemic stability, and the EU's banking sector would not thank its legislators for leaving it with a different and less flexible set of rules than its American and Asian competitors.

Theresa Villiers MEP
European Parliament rapporteur for Basle II
Brussels

Purple prose

SIR – *The Economist* regularly spots important social notes as with article on the colour purple ("Seeing purple", May 12th). One correction: Roman and other ancient purple colourings came from crushing a colourful snail. Ancient Tyre on the Mediterranean was an export centre for the colouring matter and gave it the name Tyrian purple. Roman nobility wore the colour as a fringe; commoners were not permitted to wear it—an early example of sumptuary law.

Robert Baker
Los Angeles

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Economist.com SPECIAL

Can sanctions be smarter?

May 24th 2001
From The Economist print edition

The United States is rethinking policy towards its old enemies in the Gulf. Sanctions have outlived their purpose, but they are hard to replace

UMP

Get article background

SOON after taking office, George Bush told his officials to review America's policy towards Iraq and Iran. The general idea behind these reviews was to find out if there was a way of being tougher towards Saddam Hussein's Iraq, and perhaps less tough towards Muhammad Khatami's Iran. The exercise drags on, but the results so far do not seem to be fitting the required pattern. The only part of the Iraqi rethink to emerge publicly is designed to ease United Nations sanctions against Iraq (albeit in a way that Iraq rejects but cannot prevent), while America's unilateral sanctions on Iran look as if they may well remain intact.

To discuss Iraq first. The stranger ideas being considered in the review remain under wraps: how to help Iraq's split opposition to overthrow the regime, for instance, or indicting Mr Hussein for his war crimes. But America, with Britain's help, has come up with new "smart" plans for replacing the 11-year-old sanctions. Ever since the UN's weapons inspectors were expelled from Iraq two and a half years ago, sanctions have lost their original purpose of ensuring that the country was declawed of its weapons of mass destruction (see article). They now merely help to devastate Iraq's economy and bolster its cruel dictatorship. A change is called for.

America and Britain think they have found the right one. They are hoping this week to persuade not just the other three permanent Security Council members, Russia, China and France, but also Iraq's neighbours, that there are more effective ways of squeezing Mr Hussein's regime. And they hope to do this before the current oil-for-food protocol, with its crude and leaky web of rules, exceptions, bribes and cudgels, comes up for its six-monthly renewal on June 4th.

Basically the new smart sanctions are a more flexible and, it has to be presumed, more efficient version of the oil-for-food arrangement which allows Iraq to import food and medicine and some humanitarian goods in exchange for its oil. Under the new proposals, Iraq would be able to import all the goods it wants, except for weapons and dual-use stuff.

America and Britain hope the changes will shift the blame for Iraqi deprivation

This should cut out some of the bottlenecks in the present system. The sanctions committee has vetoed almost one in five of Iraqi orders on security grounds: Iraq can buy vaccines, for instance, but may not be allowed to import the refrigerator trucks needed to transport them. Some $9 billion-worth of approved orders linger in the pipeline and $3.5 billion-worth have been vetoed. The changes, or so America and Britain hope, will shift the blame for Iraqi deprivation from the cruelty of sanctions to Mr Hussein's misrule.

Financial control of Iraq would remain firmly in UN control: all the money from oil sales would go to the UN escrow account to stop Mr Hussein spending it on weapons. This means that although the country would be able to import more, it would still be denied the free movement of labour and capital that it

desperately needs if it is at last to start picking itself up.

Sitting on the world's second-largest oil reserves, Iraq was once, politics aside, an advanced country. Now its living standards are on a par with Ethiopia's; Unicef confirms a 160% rise in Iraq's infant mortality rate since 1991; and the middle classes have disappeared. Iraq needs massive investment to rebuild its industry, its power grids and its schools, and needs cash in hand to pay its engineers, doctors and teachers. None of this looks likely to happen under smart sanctions.

Enriching the neighbours

Another problem is that the old "dumb" sanctions have made quite a few people rich, apart from Mr Hussein and his cronies. Iraq's neighbours, as well as the semi-autonomous Kurds under UN protection in northern Iraq, have earned billions of dollars from tolls, transit fees and smuggling. As an extra indirect reward, Turkey, Syria and Jordan are each getting around 150,000 barrels a day of oil sold by Iraq at bargain prices, just so it can get its hands on some cash outside UN supervision.

Thanks to this inventiveness, Iraq now has a hidden oil trade worth anything from $1.5 billion to $3 billion a year, on top of the $16 billion a year it earns officially. Jordan's shaky economy would probably have collapsed without these gifts of Iraqi oil. The truckloads of oil that pass through northern Iraq on their way to Turkey bring a tidy income to the Kurdish warlords who tax them. Turkish companies then distribute the oil at profit. Syria and Iran, bitter foes of Iraq for 20 years, have been lured into widening trade ties.

Smart sanctions are crafted on several assumptions: that there will be no more smuggling in or out; that roughly the same amount of oil continues to go to Iraq's neighbours, but through the escrow account; and that those same neighbours agree to police their borders to prevent forbidden goods getting into Iraq. But weaning these regional players from the trough, and persuading them to act as customs officers, is tricky. American diplomats have quietly proposed a range of possible rewards, in exchange for which Iraq's neighbours would place all their oil imports under the UN umbrella.

The suggestions include creating an "insurance" fund to compensate for Iraq's threatened end to oil supplies. "Any country that deals with the new American plan will lose its trade dealings with Iraq," says Tariq Aziz, Iraq's deputy prime minister, and he may not be bluffing. The fund might be financed partly by raiding Iraq's escrow account (if that is not illegal), partly by contributions from "friendly" governments and multilateral institutions. Kuwait, for instance, has said that it would "rush to the aid" of Arab countries hit by an Iraqi oil cut-off, and the United States backed the IMF's recent bail-out of Turkey.

Jordan and Turkey, America's allies, will probably go along with the new proposals. Syria and Iran may wait to see which prospect looks more lucrative, bowing to UN dictates or keeping the Iraqi back-door open. The new sanctions are also likely to involve considerable payoffs to other Security Council members.

Unseating Saddam

The contradiction is that, even as America tries to find a new way of living with Mr Hussein, it is again toying with the idea of getting rid of him. During the presidential- election campaign, Mr Bush complained that the Clinton administration was not serious about its stated policy of "containment plus regime change". He promised to be more serious himself.

Many people now in senior jobs have gone further. Paul Wolfowitz, the number-two in the Defence Department, and Richard Armitage, a deputy secretary of state, once signed an open letter calling for recognition of the Iraqi National Congress (INC), one of the main opposition groups, as Iraq's legitimate government.

But the idea of backing an insurrection usually goes down better with crusading congressmen and gung-ho pundits than with the officials and soldiers who would have to implement the policy. The Clinton administration resisted spending the money Congress had set aside for the Iraqi opposition for as long as possible, and in the end used it to buy the would-be revolutionaries fax machines.

It is difficult to imagine the prosperous Iraqi exiles who lobby Congress leading a charge on Baghdad. Once in office, the Bush administration recognised that the INC was not the only pebble on the beach. These days, the serious armed resistance to Mr Hussein comes from the Shia Muslim guerrillas in Iraq's southern swamps. But since they are supported by, and often based in, Iran, America wants nothing to do with them. Iran is the next problem.

The Khatami disappointment

The election in 1997 of Muhammad Khatami, Iran's would-be reforming president, bred hopes that America and Iran might restore the diplomatic and trade links that were severed so sharply at the time of the 1979 Islamic revolution. Not so. President Bush has already renewed America's unilateral sanctions on Iran, and in August Congress will probably renew an act imposing secondary sanctions.

American oil firms were the largest buyers of Iranian oil

Although imports into America from Iran were banned in the 1980s, American oil firms, through their foreign affiliates, remained the largest buyers of Iranian oil. Then, in 1995, Conoco concluded a huge deal to develop Iran's offshore oil. This was the last straw: Bill Clinton, announcing that all trade and investment in Iran would in future be banned, forced Conoco to pull out. A consortium led by Total, a French company, gleefully replaced it. The next year Congress passed the Iran and Libya Sanctions Act (ILSA), allowing secondary sanctions on foreign companies that invested heavily in Iran's and Libya's energy. Yet Mr Clinton waived his right under the act to punish Total, and several other non-American firms have since invested in Iran and gone unpunished.

When Mr Khatami took over, he called for "a crack in the wall of mistrust between the two nations". He made friends with some of America's Arab allies, such as Saudi Arabia; he toned down Iran's opposition to the Israeli-Palestinian peace process; he took steps to halt the murder of Iranian dissidents abroad and made some feeble efforts at social reform. In response, Mr Clinton lifted the embargo on certain Iranian exports, such as pistachios, and allowed his secretary of state to speak almost apologetically about American influence during the years of the shah. American oil companies, convinced that Iran would soon be open for business, began divvying up the best Iranian fields.

They were wrong. Mr Bush's review of policy towards Iran will not be revealed until after Mr Khatami's (almost certain) re-election on June 8th. But last month the Americans again vetoed Iran's application for membership of the World Trade Organisation. In March the president renewed the embargo on investment and trade, declaring Iran to be a threat to "the national security, foreign policy and economy of the United States". Few now expect Congress to allow ILSA to lapse when it comes up in August; the only question is whether it will be renewed for the full five years.

EPA

Iran has reformed a little, but not enough

Not yet to be trusted

Since ILSA is barely applied, it has done little harm to Iran's economy. The ban on American trade and investment has a far more damaging effect. Iran's energy sector, with ageing fields and growing demand at home, needs a vast amount of money if it is to meet its monthly OPEC output quota. (It has met it only once in the past year.) As for trade in general, many Iranian businessmen miss the energising high-tech presence of their American colleagues.

American administrations have always said they need to be satisfied on three issues before ending this particular cold war: Iran's production or purchase of weapons of mass destruction (see article); its sponsorship of terrorism; and its destructive influence on Arab-Israeli peace.

In March the State Department called Iran "the most active state sponsor of terrorism in 2000". The

Americans claim that Iran has stepped up arms shipments, by way of Syria, to Hizbullah in Lebanon—which few, outside America and Israel, now see as a terrorist organisation—and that it supports Hamas and Islamic Jihad, which do indeed carry out terrorist acts. An extremely sensitive issue is the unsolved explosion at Khobar Towers, the building in Saudi Arabia that was blown up in June 1996, killing 19 American servicemen. The Saudis say publicly that their own nationals alone were responsible; the FBI sees an Iranian hand.

However, perhaps the most important reason for the deterioration in relations is neither weaponry nor suspected terrorism, but the Palestinian *intifada*. Before the uprising broke out last September, Mr Khatami and his foreign minister pursued a relatively gentle line, and the Iranian hardliners opposed to Middle Eastern peace were isolated and demoralised.

But when the Palestinian death-count began rising, and Ariel Sharon was elected Israel's prime minister, the hardliners had their day. Mr Khatami could no longer afford to distance himself from them. A conference, organised by one of Mr Khatami's supporters, was held in Tehran at the end of April to show support for the *intifada*. It was attended by VIPs from the Islamic world and by the leaders of Hamas, Islamic Jihad and Hizbullah.

At the conference, Mr Khatami himself proposed only that there should be a "referendum" to decide Palestine's future. But Ayatollah Ali Khamenei, Iran's conservative "supreme leader", attacked Israel's "satanic intentions". In general, the conference revived Iran's old image of violent pan-Islamism. It alienated influential Americans, and made it more unlikely that America would drop its sanctions. But until those sanctions are dropped, not even moderate Iranians will agree to official talks with the United States.

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A bigger punch

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From The Economist print edition

Scuds are only the start

IRAN, like Iraq, wants weapons to defend itself in a dangerous part of the world. As a result, it threatens a wider region. With help from Russia, China and North Korea, it is building increasingly long-range missiles.

From time to time, America has imposed trade sanctions on the foreign companies involved. As a member of the missile-technology control regime (MTCR), which prohibits help to non-members for missiles of more than a certain range and capability, Russia is not supposed to help Iran, but its export controls leave much to be desired. China too has pledged to end missile help that infringes most MTCR rules, though its controls are leaky too. By now, Iran is fairly self-sufficient in building shorter-range Scud-type missiles. Its most modern missile, the 1,300km medium-range Shahab-3, could strike targets in Israel. Work on a Shahab-4 and possibly a Shahab-5 with potentially intercontinental range is also under way.

Investing in missiles makes little sense unless they can deliver a big punch. Although Iran has signed treaties promising not to build nuclear, chemical and biological weapons, it is suspected of setting up a network of companies to buy materials, technology and know-how for such weapons on the international black market. And although Iran has declared some of its chemical stocks, as required under the Chemical Weapons Convention, it is thought to hold others in reserve, including “nerve, blister, choking and blood agents”, according to recent unclassified American intelligence reports. Its pattern of purchases abroad suggests a keen interest in biological weapons too.

Meanwhile, Russia is helping to complete a nuclear power plant in Iran. America insists that this will help Iran develop expertise it can use in a weapons programme—rather as India is now known to have used foreign civilian help in building its bomb.

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The hidden menace

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What the inspectors didn't find

AFTER its defeat in the Gulf war, Iraq agreed to give up all its weapons of mass destruction and all its missiles save the short-range kind (175km, 108 miles, or less). Inspectors, working for the United Nations, were meant to supervise the dismantling of the arsenal.

Although Iraq kept trying to hide what it had, the inspectors nonetheless managed—before they were thrown out in December 1998—to dispose of large quantities of chemical weapons and many, though not quite all, of Iraq's known missiles. They also dismantled the critical elements of Iraq's nuclear-weapons programme. When the inspectors arrived, Iraq was probably within months of producing a fission bomb. The guess is that, if constraints were lifted, Iraqi scientists could build a nuclear bomb within about five years, and sooner if they could buy the highly enriched uranium or plutonium required.

However, the inspectors could not account for more than 4,000 tonnes of precursor chemicals used in the manufacture of chemical weapons, as well as more than 30,000 chemical shells and other munitions. Similarly, despite Iraq's denials, there is strong evidence that it made warheads containing VX, one of the most toxic nerve agents, and still has plenty of the stuff hidden away.

Iraq fought hardest to conceal its biological weapons. Until 1995 it denied it had ever made any, then claimed it had only tinkered. Yet inspectors found evidence of production on an industrial scale. Iraq is known to have stockpiled doses of anthrax, botulinum toxin and aflatoxin, a carcinogen. It has yet to account for some 17 tonnes of growth medium for making such weapons, and is thought to have experimented with the ebola virus and bubonic plague. Since inspections ended, Iraq has tried to import equipment that it says is for civilian uses but could be used to make both chemical and biological weapons.

It is also rebuilding parts of its missile factories and is thought to be working on longer-range missiles. It has managed to rebuild the air defences that buzz American and British planes enforcing the no-fly zones (see map). America recently accused a Chinese company of helping to upgrade Iraq's air defences, installing fibre-optic cables to link the missile batteries, radar stations and command centres. China has since admitted privately that its companies were doing work in Iraq without UN permission, although it still insists they were working on civilian projects.

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The tax cut

Victory at a price

May 24th 2001 | WASHINGTON, DC
From The Economist print edition

It's going through, but it's still too big

Get article background

Reuters

Watch those clouds

ONLY days ago, Republicans were certain that a bold tax cut would be signed into law by Memorial Day on May 28th. That would provide powerful evidence of the president's ability to carry out his radical agenda. Then, amidst the hullabaloo surrounding Jim Jeffords, the certainty faded. Getting the tax bill signed by Memorial Day no longer seemed assured. And once the bill, whatever its final shape, is law, it may mark the end rather than the beginning of the president's hopes of far-reaching reform.

The Senate passed its version of the tax bill on May 23rd, after two days of filibuster by amendment, where Democratic senators repeated their accusation that the package was excessively tilted towards the rich. As *The Economist* went to press, the tax package was in conference, a period of negotiation where it is reconciled with the versions the House has already passed. Newly emboldened, Democrats are increasingly determined that the bill should look like the Senate version.

The Senate's plan is built around the same four planks as George Bush's—cuts in marginal tax rates, an increase in the tax credit for children, a reduction of the "marriage tax penalty", and a gradual repeal of the estate tax. But there are significant departures from Mr Bush's scheme.

The Senate tax cut is smaller ($1.35 trillion over 11 years rather than the $1.6 trillion Mr Bush wanted and the House passed). The top tax rate (currently 39.6%) would fall to 36% under the Senate proposal, compared with 33% in the House version. The Senate version offers more to lower-income Americans (for instance, it makes the child tax credit partly refundable), and it includes education and pension tax breaks dear to Democratic senators. It also offers $100 billion in a short-term fiscal stimulus—something not in Mr Bush's original plan, but a goal he now touts ceaselessly.

Even if the final bill looks much like the Senate version, it would still represent a remarkable political achievement for Mr Bush. The largest tax cut since Ronald Reagan will have been passed in less than five months, far faster than the Gipper managed, despite the slimmest of congressional majorities and widespread public apathy. Opinion polls show most Americans want tax cuts, but not as much as they want better schools or cheaper petrol. Equally remarkable, the tax cut has escaped disfigurement from business lobbyists looking for special-interest tax breaks.

Much of this was due to clever politicking. The president made tactically astute, if extraordinarily disingenuous, use of the bully pulpit, suggesting to Americans that the tax cut was the answer to virtually every problem the country faced—from the slowing economy to high energy prices. Lobbyists and businessmen were silenced by the promise that this tax bill was the beginning, rather than the end, of tax cuts.

Mr Bush made highly visible presidential trips to states which he carried in November and where Democratic senators face tough re-election battles. His most important convert, Max Baucus, the top Democrat on the Senate Finance Committee, is up for re-election next year, and he comes from Montana, a state that voted heavily for Mr Bush.

The Bush team also had some outside help. The jump announced in January in the projections of the ten-year surplus (from a cumulative total of $4.6 trillion to $5.6 trillion) made it increasingly hard to argue—at least within the parameters of the Washington debate—that tax cuts were unaffordable. Alan

Greenspan's public support was another big boost.

Above all, for most of the tax-cut battle, the Democrats were in disarray. The party's leaders never found a way around the fact that individual components of Mr Bush's plan, such as the marriage tax penalty, were extremely popular even among Democrats.

All this politicking has tended to obscure whether the tax cut makes economic sense. The current package might be said to be an accountant's tax cut rather than an economist's one. It is defined by the arbitrary numbers of a ten-year horizon for the budget surplus. These numbers alone are dubious: few Washington realists regard the projected levels of government spending as tenable. Looking beyond the ten-year horizon, towards the retirement of millions of baby boomers, the tax cut looks increasingly imprudent.

Even more bizarre, this accountant's approach has led to absurd micromanagement of future fiscal policy. In the Senate version of the bill, for instance, the college-tuition tax credit is introduced in 2002 and ended in 2005. The estate tax is repealed—but only in 2011, to disguise the long-term cost of losing it (and, naturally, to make those numbers balance). Marginal tax rates are lowered mainly in the later years. To comply with obscure Senate rules, the entire tax bill is technically revoked in 2011. (Presumably, that will not happen really.)

Economists tend to judge tax policy on its efficiency (how little a tax distorts economic activity), equity and simplicity. Democrats have spent a lot of time arguing that this package is unfair. Less noticed is that the tax package does surprisingly badly on the other two criteria.

Particularly if the Senate succeeds in limiting the reduction in the top rate of income tax, this tax package may not do much to boost long-term growth. It is also hard to argue that it makes America's tax code simpler. And it has certainly made more radical tax reform harder.

The lure of tax cuts may not be available to future presidents and Congresses to sugar-coat tax reform. Meanwhile, by doubling the child tax credit, the administration has created a powerful new reason for Americans to stick with the current (overcomplicated) system. Add all these factors together, and history may judge Mr Bush's tax-cut victory as rather a Pyrrhic one.

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The Los Angeles police

A watching eye

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From The Economist print edition

At last, an outside monitor?

COMPLIMENTS come cheap in campaign season, but the officers standing at the back of the meeting still grin when the candidate announces that Los Angeles has the “finest police department in America”. On the stump, both James Hahn and his opponent Antonio Villaraigosa pay their respects to the Los Angeles police. But whichever of them is elected mayor on June 5th will have to tackle the problems of an institution with, it seems clear, too proud a tradition of independence.

An early decision for the new mayor will be whether to appoint Bernard Parks to a second five-year term as chief of police. At a debate on May 19th in Crenshaw, Mr Hahn’s home turf and a predominantly black part of the city, both candidates raised cheers with their praise for Mr Parks, who is himself black and is seen as a bulwark against racism in the Los Angeles Police Department (LAPD). Still, neither candidate would promise to reappoint him, insisting that the decision would depend on what he does to reform the force.

The main test of this will be Mr Parks’s commitment to a “consent decree” issued last October in settlement of a lawsuit brought by the federal Justice Department. The suit, which alleged a “pattern or practice” of misconduct by the LAPD, was prompted by revelations of corruption in an anti-gang unit known as CRASH, Community Resources Against Street Hoodlums. The decree sets up a system for investigating shootings by officers, and a way of keeping track of police-conduct reports (and thus providing early warning of officers turning bad). It also joins the calls for an outside eye to keep watch on the force’s operations.

The decree is not yet in effect. The judge involved held back from enforcing it until a monitor was chosen. This should have been done by March 1st, but the city council dithered until, on May 18th, it eventually picked Kroll Associates, a security firm whose boss, a former New York prosecutor, will lead the monitoring team. The judge still has to approve of the choice.

Messrs Hahn and Villaraigosa, both Democrats, have embraced the consent decree much more warmly than the current mayor, Richard Riordan. Like Mr Parks, Mr Riordan abandoned his opposition to the idea only when it became clear that it had enough support in the city council to override their wish to do all reform internally.

The LAPD needs outside monitoring because it has proved unable to reform itself. The terms of the consent decree resemble part of a much longer list of changes suggested in 1991 by a commission led by Warren Christopher, a Los Angeles lawyer who went on to become secretary of state, after officers were filmed beating a black man, Rodney King. Those suggestions had in turn echoed proposals made after the Watts riots in 1965. None of these earlier recommendations was adopted.

The more recent Justice Department investigation followed allegations by Rafael Perez, a CRASH officer in Rampart, a poor, predominantly Latino part of the city. In exchange for lenient treatment after he was arrested for stealing cocaine from a police-station locker, Mr Perez confessed that he and another officer had shot unarmed men and then planted guns on them. He claimed that fabricating evidence and falsifying testimony were standard practice in CRASH, which saw itself as the outfit that “intimidates those who intimidate others”.

Crash reports

His revelations and accusations have devastated the city’s law-enforcement system. So far 100 convictions in which Mr Perez was involved have been overturned, and $30m paid out in compensation. Lawyers estimate that the final damages may run to $100m. Seventy officers are under investigation.

Morale has plummeted.

Yet most people in Los Angeles seem less worried by the Rampart scandal than they were by the Rodney King beating, even though the former involved more victims. Rough stuff, it appears, is less troubling when the victims are gangsters. Since their release, several of the gang members fitted up by CRASH have been shot by rivals or arrested on fresh charges. On March 13th a man crippled and then framed by Mr Perez was arrested in Las Vegas for drug possession, producing more shrugging of shoulders. And gang violence has risen in the past year, after steadily dropping for a while.

Both mayoral candidates therefore balance their support for the consent decree with plenty of tough noise about crime. Each is quick to emphasise that he believes most of the LAPD's officers are honest. Almost the only difference between Mr Hahn and Mr Villaraigosa is a minor argument about whether the force should introduce a working week of three 12-hour days for some officers. Mr Hahn is in favour, thus buying himself the endorsement of the police union. Mr Villaraigosa is against, although he does countenance trying out a week of four ten-hour days.

Saying the right thing about police hours may help to decide the election. Once in office, though, the next mayor will have more to worry about than keeping the cops at the back of room smiling. Los Angeles needs a police force that lives up to its promise to "protect and serve" the city without bringing disgrace on it.

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The Rev Al Sharpton

Black America's new champion

May 24th 2001 | NEW YORK
From The Economist print edition

He's running for president

AP

Leadership in action

THE Rev Al Sharpton confessed to a secret fantasy this week: "the day Rudy Giuliani has to say 'Good morning, Reverend Mr President'." Cynics might jibe that most people with Mr Sharpton's history would probably be on the run, not planning to run for America's highest office. As it happened, on May 23rd he was sentenced to 90 days in jail for trespassing on navy land during a protest against military exercises. The offence was added to several prior arrests for civil disobedience in New York.

Notwithstanding that, and although his chances of becoming president remain mercifully small, Mr Sharpton decided this week to run for the Democratic nomination. This declaration marks another milestone in his attempt to replace Jesse Jackson as the country's leading left-wing black politician.

Mr Sharpton's rise is a remarkable story of triumph over adversity, much of it self-inflicted. Yet, ironically, without his frequent scrapes, he would probably never have achieved his current prominence. Starting out as a preacher in Brooklyn at the age of four, he later became youth director of Mr Jackson's Operation Breadbasket. He is close to both James Brown, the godfather of soul, and Don King, the godfather of boxing (indeed, he has just helped organise a concert for Mr Brown in Beijing next month before a boxing match promoted by Mr King).

In Mr Sharpton's favour stand a sharp wit, courage and a remarkable talent for publicity. But these have often been used to ill effect. In 1987, he supported claims—later discredited—by Tawana Brawley, a teenager, that she had been gang-raped by white men, including law-enforcement agents. He still has not apologised to Steven Pagones, a prosecutor whom he accused of taking part in the rape. However, his $87,000 debt to Mr Pagones resulting from a defamation suit has now been paid—most of it by prominent black businessmen and Johnnie Cochran, O.J. Simpson's lawyer. They hope that this puts the case behind the aspiring president.

In 1991, he survived a stabbing during a march through Bensonhurst, where a black teenager had been killed by a white mob. In 1995, he talked about the need to oust the "white interloper" from Harlem, and his supporters marched daily outside Freddy's Fashion Mart, a non-black-run store there, chanting about "blood-sucking Jews". This ended violently when a protester shot and wounded three whites and a Pakistani, and then started a fire that killed eight people, including five Latinos.

Mr Sharpton's renaissance began when he led peaceful protests against the shooting of Amadou Diallo by the New York Police Department in 1999. By early 2000, aspiring candidates Hillary Clinton and Al Gore had visited him for a blessing. Late last year, Mr Sharpton increased his national presence, protesting at an execution and at the Florida recount. He intends to make the Democrats' mishandling of that recount a big theme of his campaign.

This year Mr Sharpton has tried to repeat the Diallo protests in Cincinnati, where rioting followed the police shooting of an unarmed youth. And, to establish himself as an international statesman, he has travelled to Sudan to highlight the problem of slavery—and plans to return soon, accompanied by Michael Jackson. In a remarkable display of political maturity, he even decided to stay away from the trial earlier this year for gun possession of rapper Sean "Puffy" Combs.

His return to polite society has been marked with a flattering cover story on the "post-Sharpton

Sharpton" in the *New York Times* magazine. "History has plopped him in a very large spotlight on a very empty stage." *Gotham* magazine investigated what happens when you take Mr Sharpton to "a society restaurant and surround him with intriguing people". Answer: it's fun.

This week's presidential announcement was, in part, a sly way of confirming that Mr Sharpton will not run for Mayor of New York. In 1997 he polled 32% in the Democrat primary. This year, he hopes to dominate that race from the sidelines.

But his real aim is to replace Jesse Jackson. Mr Jackson's star has been waning this year. First came the news that he had fathered a child in an adulterous relationship. Then there were claims that Mr Jackson's family has benefited financially from his political campaigns against companies with too few black employees. Mr Sharpton's campaign of damning Mr Jackson with faint praise has been awesome (eg, comparing Mr Jackson to Muhammad Ali, who "can't fight no more, but he's still a great champion").

Being the leader of black America means less than it once did. A growing number of blacks, particularly middle-class ones, are appalled by what Mr Sharpton stands for. But he may be capable of mustering enough votes in the presidential primaries to exert a powerful leftward influence on Democrat policies. Mr Bush should wish him well.

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Control of Congress

What one man can do

May 24th 2001 | WASHINGTON, DC
From The Economist print edition

Jim Jeffords's defection from the Republican Party is a cruel blow to the president

Reuters

FOR two days or more, he kept everyone on tenterhooks. Jim Jeffords, the senior Republican senator for Vermont, sent strong signals, through the usual array of anonymous sources, that he was planning to abandon his party. On Thursday, in Vermont, he made it official: he is to become an independent and will caucus with the Democrats. With that single step, he makes the Democrats the majority party in the Senate.

The Democrats had fought to get him, and the Republicans to keep him. Tom Daschle, the Democratic leader, reportedly "giddy" with excitement, offered Mr Jeffords the chairmanship of a powerful Senate committee. Trent Lott, the Republican leader, promised to trump any Democratic bribe. The Republicans also tried to persuade Zell Miller, a Georgia Democrat who frequently votes with the administration, to switch to the Republican side. Their efforts were in vain.

Mr Jeffords is one of the last surviving examples of a Rockefeller Republican, that breed of north-eastern blue-blooded Republicans who used to dominate the party but who have been increasingly marginalised by the more conservative figures who hail from the South and the west. He voted against Ronald Reagan's tax cut in 1981, supported Bill Clinton's health reforms in 1993-94 and was maddened by George Bush's decision to govern as if he had a clear mandate for a conservative agenda.

But the squabble also became personal. The administration punished Mr Jeffords for his opposition to tax cuts by refusing to invite him to a White House ceremony honouring a Vermont native who had been voted teacher of the year. It also hinted that it might oppose the dairy subsidies that are particularly important in Vermont. Naturally, Mr Bush cannot be seen to be kowtowing to every powerful senator with a bee in his bonnet. But snubbing and threatening him is never a sensible course.

Mr Jeffords's departure has robbed the Bush administration of its momentum. He has reminded everybody of two awkward facts: the difficulty of keeping the Republican coalition in one piece (other moderate north-easterners, including Lincoln Chafee and Olympia Snowe, are also uncomfortable with southern-fried Republicanism); and the frailty of the Republican majority. Another Republican senator, Jesse Helms, is in poor health, and Strom Thurmond is showing his 98 years.

Mr Jeffords has already shown other would-be mavericks that the price of loyalty can be astronomical. He played a key role in forcing Mr Bush to reduce his tax bill from $1.6 trillion to $1.35 trillion, and in securing guaranteed funding for the education of disabled children, his personal hobby-horse. In fact, Mr Jeffords has voted with Democrats over the years more often than any other Republican, so he should feel at home with them.

He has, of course, technically decided to become an independent. This was a sop perhaps to his constituents, who pride themselves on the orneriness of Vermont and already have another independent, Bernie Sanders, once the socialist mayor of Burlington, in the House. Nonetheless, his alliance with the Democrats still makes them the majority party. Mr Daschle will replace Mr Lott as majority leader (and the hapless Mr Lott may be challenged for the leadership of the Senate Republicans). Democrats will acquire the chairmanship of Senate committees, giving them the ability to control legislation.

This is calamitous news for the Bush agenda. On Wednesday the Senate passed Mr Bush's revised tax package (with Mr Jeffords voting in favour). But henceforth Mr Bush will surely have to water down his agenda to suit the new Democratic majority in the Senate. He will have to kiss goodbye to his dream of

stocking the federal judiciary with right-wingers. And other appointments may suffer too. Ted Olson's chances of becoming solicitor-general look slimmer by the day.

Mr Bush will also have to change what he means by "bipartisanship". So far he has been able to pick off conservative Democrats to give a bipartisan sheen to conservative legislation. Now that Mr Jeffords has jumped ship, he will have to deal with the Democratic leadership.

The Democrats are as delighted as the Republicans are downcast. They have been hopelessly adrift since the election, furious about having the presidency snatched from them, embarrassed by the continuing Clinton scandals, and outmanoeuvred by the White House. Capturing the Senate majority makes it clear where the party leadership lies: with Mr Daschle and, to a lesser extent, Ted Kennedy. The Democrats used their control of the Senate to destroy the last Bush presidency. Mr Jeffords may give them the opportunity to do the same thing to the present one.

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Texas and water

Pay up or dry up

May 24th 2001 | AUSTIN
From The Economist print edition

Another state trying not to go thirsty

OIL built Texas, but water will shape its future. With five droughts in the past four years, water is running out fast. The Rio Grande, one of the state's main sources, has failed to reach the Gulf of Mexico for the first time in about 50 years. And demand is soaring, with the number of Texans expected to double by 2050. If this goes on, El Paso will run out of water in 20 years and other cities not much later.

AP

Not this groundhog's day

Can the supply be increased? Texas has been squabbling with its neighbours about the division of the Rio Grande's water. There is talk of new reservoirs, but they may not be ready before El Paso and other cities have gone dry. Since surface water is so scarce, many people want to pump more water from underground aquifers. This would help—55% of the state's population already depends on such water for drinking and agriculture—but reliance on well water, if not handled carefully, could create vast environmental problems and leave the state with no water reserves.

So Texas is again wondering how to cut demand. Nobody can stop the state's population growing. But there are surely ways to limit the amount of water each Texan uses. Americans consume more water per head than most people, yet the price (a third of a cent per gallon) is lower than in most other rich countries. Water takes up less than 0.8% of the average American household budget. In theory, a price increase could achieve two things. It could raise money to help build better pipelines. It could also tame consumption, perhaps by as much as 20% in some areas.

Meanwhile, however, T. Boone Pickens, an erstwhile corporate raider, has been working on the supply side. He has been busy buying water rights in western Texas, setting up a consortium of landowners who have agreed to sell him their water at a given price. Mr Pickens hopes to pipe 150,000-200,000 acre-feet of water from the vast Ogallala aquifer in the Texas Panhandle to the state's parched cities. (An acre-foot, enough water to cover an acre a foot deep, is 326,000 gallons, or some 1.2m litres.)

The cities would pay on a sliding scale, depending on the distance Mr Pickens has to pump the stuff. Far-away El Paso would pay $1,400 per acre-foot, Dallas around $800. Much of the projected revenue of $200m would go into building pipelines to carry the stuff. But these are still stiff prices: the state of California recently paid $260 an acre-foot in a similar deal.

Environmentalists have reason to worry, too. The Ogallala replenishes itself at a rate of less than one acre-foot a year. In these circumstances water extraction is little different from mining. Indeed, Texas law treats water much as it does oil or gold: anybody who has access to the stuff can extract as much as he wants.

In theory, such water is protected by Texas's Groundwater Conservation Districts. But the state's strong tradition of property rights limits the GCDs' ability to control men like Mr Pickens. C.E. Williams, general manager of the Panhandle's Groundwater Conservation District No. 3, which deals with Mr Pickens, thinks the current crisis justifies pumping up to 50% of the Ogallala. But Mr Pickens's methods, he argues, would empty it within 25 years.

Mr Williams is pinning his hopes on a bill that is currently being discussed in the state legislature. This would allow more GCDs to be established, and empower them to levy a fee of at least two-and-a-half cents per 1,000 gallons to study the effects of pumping and set up replenishment projects. The only trouble is, Mr Pickens may have already got himself exempted from the fee.

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Rumsfeld's defence

May 24th 2001
From The Economist print edition

His plans for military reform have been roundly—and wrongly—condemned

AS GEORGE BUSH prepares to unveil what is likely to be the most wide-ranging military reform for decades, a strange conventional wisdom is forming in Washington. It goes like this: Donald Rumsfeld, the defence secretary, has been stealthily setting up a Hillary Clinton-like policy review. By shutting important constituencies out of his defence plans, he has foolishly caused a backlash against those plans even before they have been made public. The result is that he is being forced to scale back his earlier vaulting ambition and if things go badly could even end up watching his defence review suffer the fate of Mrs Clinton's health-care plan: it will be dead on arrival at Capitol Hill.

Parts of this picture are indeed accurate. And, given the uncertainties in Washington at the moment, defence reform may end up in the bin. But the conventional dismissal of Mr Rumsfeld is premature and, on balance, is likely to be wrong.

If anyone can push through fundamental reform of the most powerful armed forces in the world, it is Mr Rumsfeld. He has long been a believer in the main bits of the new defence agenda: an increase in small, ultra-high-tech, manoeuvrable weapons at the expense of large, heavily armed land divisions; a further shift in the Pentagon's focus away from Europe towards Asia; and a change to the policy of preparing to fight two wars at once. As a central figure in his review, he picked Andrew Marshall, a Pentagon guru who has supported these ideas even longer than he has. And Mr Rumsfeld has the bureaucratic experience to fight off the Pentagon's ingrained opposition to change. Unlike any of his predecessors, he has served as defence secretary before.

So he must have known a backlash was inevitable. Last week, the joint chiefs of staff held a closed-door meeting in the Pentagon to vent their spleens against a review which, they complain, has shut them out of important decision-making. A former army chief of staff, General Gordon Sullivan, went public with the army's anxieties by lambasting Mr Rumsfeld. Expressions of military alarm matter because even if he were to have his reform plans approved by politicians, Mr Rumsfeld must still rely on the Pentagon to implement them.

But how many of his reforms will be approved? The noises coming from aggrieved senators suggest not many. Angry at not being consulted enough, the Republican leadership in the Senate recently held up three of Mr Rumsfeld's nominations for senior jobs at the Pentagon—a slap in the face, since it is usually the opposition party that makes life awkward for the administration by deferring appointments.

At the moment, Mr Rumsfeld is being attacked not for his decisions but for the process he set up to make them. The defence secretary established a score of working groups in the Pentagon, which were told to

make specific recommendations on specific questions, but not to involve themselves in the overall picture. The secretary, along with his deputy, the president and the vice-president will assemble the pieces into a (with luck, coherent) whole. This is known as leaving everyone in the dark.

Such a process does have shades of Mrs Clinton's health-care fiasco. But it does not mean Mr Rumsfeld is in the wrong—either in principle or in practice. The Pentagon chiefs have no God-given right to determine American defence policy in advance. The country has civilian control of the military. As for those controllers in Congress, they will get every opportunity to pick the strategy apart when it is presented to them.

It also seems unfair to criticise Mr Rumsfeld for not defending his decisions before he has fully made up his mind. Previous reform efforts were derailed because, in the name of open consultation, defence chiefs and politicians were drawn into the review process too early. Bill Clinton's first defence secretary, Les Aspin, wanted to look at whether America could move away from its two-war strategy to something called "win-hold-win" (fight one war to victory, run a holding campaign in the other, then seek to win that). His critics derided this as "win-hold-oops", before the details were thrashed out, and had the idea squelched. Now many are prepared to support it.

In so far as opposition to Mr Rumsfeld is based on offended *amour propre*, it seems likely to fade. The real problems will come from those who lose out from the substance of the reform—notably the army, its backers in Congress and, in particular, congressmen with military bases in their districts. The grumbling and growling in the Senate clearly shows that there will be a battle over military reform (there always is). But it is wrong to conclude that Mr Rumsfeld is likely to lose the fight.

With two ex-defence secretaries and a former chairman of the joint chiefs of staff in the cabinet, it will be hard for opponents to argue that the Bush administration does not understand the military. More important, the new defence policy does not require an immediate choice between, say, building space weapons and junking aircraft carriers on the one hand, and continuing with the existing military structure on the other. For the next few years, much of the so-called "revolution in military affairs" will be pursued by increases in R&D spending, which would amount to 3% of the annual defence budget even if the most starry-eyed proponents of the revolution get their way (which they won't). The hard choices occur only later. Mr Rumsfeld's current tactics may even be a feint to secure passage of just such an R&D increase in exchange for not cutting existing programmes as much as the opponents fear.

In the end, Mr Rumsfeld is subject to his own civilian control. It will be Mr Bush who sells the defence plans to Congress. And it will be Mr Bush who decides whether to fight for these plans or for, say, Social-Security reform. Mr Bush may yet choose not to engage in a battle with the Pentagon and its allies. That would be Mr Rumsfeld's problem. It would hardly be his fault.

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Abortion

Is a fetus a person?

May 24th 2001 | COLUMBIA, SOUTH CAROLINA
From The Economist print edition

The old argument won't go away

REGINA MCKNIGHT, a 24-year-old drug addict, has been sentenced to prison for 12 years in South Carolina. Miss McKnight smoked crack cocaine in 1999 while she was pregnant. Her unborn baby died in the eighth month. Miss McKnight, who has three other young children and is now pregnant again, has been convicted of homicide.

South Carolina is the only state where, by law, a fetus able to live outside its mother's body is considered a person with legal rights. This law is not of long standing, but the result of a court decision of 1997. Abortion advocates see it as a particularly egregious part of widespread attempts by anti-abortionists to establish fetal rights in any area of law they can. Their purpose, says the pro-abortion camp, is ultimately to overturn *Roe v Wade*, the 1973 Supreme Court ruling that made abortion legal in America.

For years, various state legislatures have been chipping away at *Roe v Wade* by passing laws that make it more difficult for women to obtain abortions. But abortion supporters fear that, with George Bush in the White House, *Roe v Wade* itself may be overturned if the new president, who opposes abortion, is able to place enough like-minded justices on the high court. (Mr Bush implied during the campaign that he would not overturn it, but would respect settled law; many do not believe him.)

The Supreme Court has so far been silent on the issue, declining to hear an appeal of the original 1997 South Carolina case. *Roe v Wade* ruled that, in the third trimester of pregnancy, the state had such a compelling interest in protecting the life of the unborn child that it could forbid abortions. The justices in 1973 stopped short, however, of calling the unborn fetus a person at any stage.

So far, nearly two dozen other states have rejected the criminal prosecution of pregnant women for behaviour that harms their fetuses. This includes the Florida Supreme Court, which ruled five years ago that a pregnant woman who had shot herself in the stomach could not be charged under a homicide statute. But South Carolina soldiers on.

The thin-end-of-the-wedge argument against the South Carolina law is, however, less compelling than the unfair way it works in practice. It is mainly applied against drug addicts. Women who drink or smoke or drive recklessly while pregnant, and then deliver a stillborn child, are not being arrested; perhaps because many of them are well-to-do and white and not, like Miss McKnight, poor and black.

Affirmative action

The man who started it all was Charlie Condon, who used to be Charleston's prosecuting attorney. In 1989, Mr Condon began to get drug-abusing pregnant women arrested for child abuse when they turned up for pre-natal treatment at a Charleston public hospital. All the mothers arrested were poor, and nearly all were black; several later served jail terms.

Mr Condon, a conservative white Republican who rode the attendant publicity to victory several years later in the election for state attorney-general, discontinued the policy in 1994 when ten women filed a lawsuit. The Supreme Court ruled in that case, *Ferguson v City of Charleston*, that hospitals could not test pregnant women for drug abuse and then inform the police without the women's consent.

Mr Condon, who has perfected the art of self-promotion, praised the McKnight verdict and has announced that he will run for governor next year. Only a handful of South Carolina prosecutors have followed his lead and brought charges against pregnant women who are drug addicts. Some say they use the threat of prosecution to persuade the women to get drug treatment. But South Carolina has few drug-treatment programmes for the poor, and current budget problems may oblige the state to cut back even on those.

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The drug war

The struggle to exterminate a much-loved Andean shrub

May 24th 2001
From The Economist print edition

Efforts to wipe out the coca crop and stop the flow of cocaine are attracting more money and more allies than ever before. Will they work?

Get article background

Reuters

IN THE next few days, American officials are due to decide whether to restart surveillance flights over Peru and Colombia aimed at denying the freedom of the skies to light aircraft used by drug traffickers. These flights were suspended last month, after Veronica Bowers, an American missionary, and her baby were killed when their aircraft was strafed by a Peruvian air-force jet. Despite unease in the United States Congress, the likelihood is that President George Bush's government will recommend that the flights should resume. That is because they are an integral part of an ever more elaborate effort, started over two decades ago, to cut the flow of cocaine from producer countries in the Andes to consumers in the United States.

John Walters, Mr Bush's choice for the post of "drug tsar", is a strong supporter of such "supply-side" anti-drug programmes. In the Andes, these have three parts: eradication of coca, the shrub from whose leaves cocaine is extracted; the closing down of processing laboratories and trafficking rings; and alternative development, or helping coca farmers to earn a living in other ways. The death of Mrs Bowers and her daughter brought home to ordinary Americans just how much their country's "war on drugs" in the Andes has come to resemble a real war, complete with civilian casualties and some less-than-attractive allies, such as Vladimiro Montesinos, Peru's fugitive former intelligence chief who first put the shoot-down policy into practice. The missionary's aircraft had been picked out by a spy plane operated by an American crew under contract to the CIA. Investigators are likely to report that the spy plane's crew tried to warn the air-force jet not to attack. Even so, private contractors may be subjected to tighter rules and regulation in future.

American officials say that the shoot-down policy is less important than it was when it began in 1994. That is partly because Peruvian traffickers have found other routes, but mainly because most coca production has moved to Colombia (see map). That, and the presence of guerrilla armies in Colombia's main drug-producing areas, led the United States last year to grant $1.3 billion under what it called Plan Colombia, to be spent on a new anti-drug army brigade and helicopters, and on development and human-rights projects.

But the drug fighters are likely to want to resort to aerial enforcement once again. Last week American officials unveiled a request to Congress for $882m for anti-drug programmes in and around the Andean region in 2001-02. This continues Plan Colombia, but in modified form.

Adios, Plan Colombia

One change is lexical. Plan Colombia has been criticised for being likely to plunge the United States into a "new Vietnam". It is now being rebaptised as the Andean Regional Initiative. A second change is designed, say American officials, to meet the criticism that Plan Colombia is too militaristic, and risks pushing drugs and violence into neighbouring countries. So now the money is to be split roughly equally between law enforcement and development, and with the neighbours getting slightly more than Colombia. The new plan is intended to sustain the assault on Colombia's coca industry while preventing its revival in Peru, Bolivia and elsewhere. So it involves extra dollops of aid for Peru, Bolivia and Ecuador, for development as well as enforcement, and smaller sums for Brazil, Panama and Venezuela.

Will it work? American officials say that, for the first time, their effort to cut drug supply in the Andes is being backed with serious money. A report last week by the United Nations Drug Control Programme (UNDCP) suggested that the tide may be about to turn in Colombia: using different methodology from that of the United States, it reckoned the country had 163,000 hectares (402,000 acres) of coca last year, an increase of only 2% over 1999. Since then, police, backed by the American-trained brigade, have sprayed about 35,000 hectares with herbicide.

Nowadays, Latin American governments are less hostile than in the past to the United States' drug war. That is partly because of the increased aid. Peru could get around $200m this year, dwarfing its own anti-drug budget. And Latin Americans are aware that for their countries the overall costs of the drug trade—in violence, corruption and rising drug consumption—outweigh any economic benefit.

Peru's government is anxious to resume surveillance flights. But even more striking has been the change in Mexico: Vicente Fox's government has shown itself to be far more willing than its predecessors to co-operate with American efforts to crack down on drugs.

But there are limits to co-operation. "What the United States calls a regional approach means us dealing with each country separately," says Michael Shifter, of the Inter-American Dialogue, a Washington think-tank. "There's still a lack of the Latin Americans working among themselves and the United States being part of that."

Forcible coca eradication is particularly unpopular. In Bolivia, where eradication and alternative development have gone furthest, unemployed former coca farmers have swelled protests against the government of Hugo Banzer. Peru's government is continuing with its predecessor's policy of forced eradication of coca in national parks; this month coca farmers in Aguaytia staged roadblocks in protest. In Colombia, the government in February halted aerial spraying in the southern province of Putumayo, where almost half of the country's coca crop is grown. Since then, officials have stressed voluntary eradication and alternative development.

Economics, too, conspires against the anti-drug warriors. All the Andean countries have recently suffered recessions, or sharp slowdowns in growth. Worse, the price of coffee, which is grown in similar places to coca, has slumped because of world overproduction, which may induce farmers to switch to coca. In Peru, coca production has been rising again since 1999, according to the UNDCP. The Apurimac valley, where there have been many efforts at alternative development since the mid-1990s, is once again "a sea of coca", according to Hugo Cabieses, an adviser to coca farmers.

Despite the drug war, total coca production is more than enough to meet demand, and the flow of cocaine is unstaunched. The anti-drug warriors may be richer, but they still face a Sisyphean task on the Andean hillsides.

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Mexico and the United States

Sex, death and desert snafus

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A new plan to help migrants stirs passions

IT HAS been dubbed “the happy box”, and is the latest wheeze from President Vicente Fox’s government to help Mexicans who illegally cross the border into the United States each year. The plan, costing $2m, is to furnish 200,000 of them with a survival kit: a box containing medicines, bandages, anti-dehydration powder, water and emergency rations to help on the dangerous trek across the deserts that straddle the border. But 25 condoms?

“Anything that helps migrants is good,” says Roberto Martinez of the American Friends Service Committee, a Quaker organisation, who works with immigrants in San Diego. “But I don’t think this will stop people dying.” Across the border, Victor Clark, director of the Tijuana-based Binational Centre for Human Rights, is more scathing. “Carrying these boxes will be like wearing a sign saying ‘I’m an illegal immigrant.’ And why the condoms? The last thing you want to do when you’ve just crossed the border is have sex.”

According to American offcials, 369 people died trying to cross the frontier last year, mainly of hunger or thirst. But at least migrants are no longer routinely robbed or beaten up by the Mexican police before they reach the border. Special units, called Beta Groups, now patrol busy crossing-points to protect migrants. Helping them survive the crossing seems a sensible next step—and all part of recognising that migration is an economic, not a criminal, phenomenon.

Past governments handed out some survival kits. Their revamp is the brainchild of Juan Hernandez, who heads a new presidential office to help migrants. He has swiftly backtracked on the condoms, saying that the box’s precise contents are still being discussed. More worrying is that press reports of Mr Hernandez’s plan seemed to take his colleagues by surprise. Never heard of it, said the foreign ministry. No budget for it, claimed the immigration office.

Mr Hernandez’s job is just one of several new posts created by Mr Fox. But his government does not yet seem to have worked out how to co-ordinate new agencies with existing ones. Given that they were created to tackle Mexico’s most pressing problems, that is not a happy sign.

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Brazil's energy crisis

St Peter is innocent

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As in California, botched regulation lies behind an electricity shortage

FACED with a looming energy shortage, Brazil's government this week announced final details of emergency measures aimed at cutting electricity consumption by 20%, and intended to avoid regular blackouts. Contrary to an earlier promise by President Fernando Henrique Cardoso, consumers who exceed their electricity quotas face heavy fines, or even temporary disconnection. To give the electricity companies more time to prepare, the start of rationing has been postponed to July. But Brazilians are already counting the cost to the economy. And consumers' groups have started winning court injunctions against rationing; the attorney-general says he will deploy up to 600 lawyers to get them reversed.

Reuters

The candle makers respond to market signals

Mr Cardoso blames the energy shortage on St Peter, whom Brazilians traditionally credit with controlling the weather. He says an exceptional drought is draining the country's hydro-electric dams, which supply nearly all its electricity, at a time when the economy, and thus electricity demand, is growing. In the past four years south-eastern Brazil—which includes Sao Paulo, its chief industrial state—and the north-east have had their lowest rainfall since the 1970s. Climate change? Meteorologists say they cannot yet be sure.

Power shortages have looked imminent several times in recent years, but just enough rain has fallen to avoid them. That has encouraged official complacency. In fact, southern Brazil has had above-averge rainfall in the past year; the dams there are full. But a failure to expand the transmission grid limits the export of electricity from the south to the industrial heartland. Since erecting power lines is far quicker than building power stations, expanding the grid is the "priority of priorities", says Adilson de Oliveira of Rio de Janeiro's Federal University.

Officials want private firms to pay for and build new lines. If they do not start doing so quickly, the government will pay for the job itself. Some left-wingers blame privatisation for the current fiasco. But the opposite is closer to the truth. Most of Brazil's electricity generation is still owned by the federal or state governments. Faster privatisation would have freed the industry from government spending constraints, allowing swifter expansion.

Partial privatisation has gone hand-in-hand with Californian-style bungling of tariffs. Under their contracts with the regulator, the electricity firms are meant to be able to pass on to customers any rise in the cost of gas. But the generators complain that in practice the regulator has not let them fully pass on a recent cost increase, caused partly by the weakening of Brazil's currency, the *real*, against the dollar, in which gas is priced.

As a result, few of the 55 new gas-fired power stations that the government wants private firms to build have got off the drawing-board. The government has promised to fix the tariff problem, but has procrastinated over doing so.

Officials hope that a few months of economising will see Brazil through until the start of the rainy season in November, and that, by next year, generating and transmission capacity will have expanded enough to prevent shortages. But is a 20% cut in power consumption achievable? Not without pain, says Mr de Oliveira. Households will have to do without such comforts as freezers and air-conditioners. And electricity-guzzling industries, such as aluminium smelting and steel making, are likely to have to reduce output.

Economists have cut their forecasts for economic growth this year. Rodrigo Azevedo of CSFB, an investment bank, had expected growth of 4.1%, but reckons it will now be perhaps one percentage point less. Others are gloomier. Since many energy-dependent industries are exporters, the trade balance will be hit too. All this has caused the *real* to weaken further, putting the Central Bank's inflation target at risk. As a result, on May 23rd it raised interest rates, for the third time this year.

The economic pain will be greater still if consumers ignore the government's pleas to economise, triggering blackouts. But the government's palpable panic seems to be scaring consumers into cutting back. Electricity firms say demand has fallen in recent days, though not yet by 20%. As they switch off the lights, many Brazilians will also be praying to St Peter for an unseasonal downpour.

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Politics in Colombia

Limits to reform

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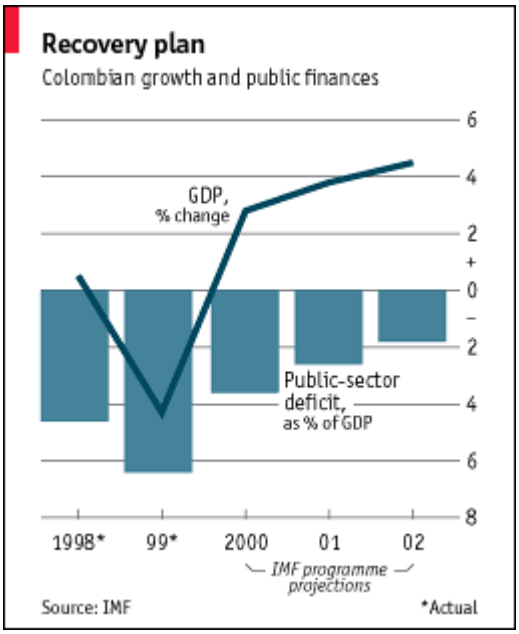
Time is starting to run out for the government

ANDRES PASTRANA has never been short of problems. Since becoming president in 1998, he has grappled not just with a drug-fuelled internal war, but with Colombia's first economic recession since the 1930s and public disenchantment with a self-serving Congress. Now his efforts to deliver reform are being rebuffed.

With the help of the IMF, a devaluation and higher oil prices, the economy bounced back quickly last year (see chart). But growth remains weak, private investment is slow to recover, and the government is struggling to cut its fiscal deficit.



Last year, the government hit its fiscal target by raising taxes and trimming its budget. But in the medium term fiscal solvency depends mainly on reforming both the system of transfers from the centre to local governments and the country's state pension schemes. A constitutional amendment to restrict transfers is now close to final approval in Congress, having passed the Senate last week. But it has been diluted. The government wanted transfers to be pegged to projected inflation plus 1.5%, indefinitely. Congress changed this to past inflation, plus 2% a year, rising to 2.5% from 2006-08, with no limit thereafter. The savings the finance ministry had hoped for over five years will now take seven, it says.

As for pensions, the government wants to raise both contributions and the retirement age, and to eliminate special regimes for members of Congress, teachers, oil workers and the armed forces. The need for reform is clear: government spending on pensions rose from 0.8% of GDP in 1991 to 2.3% in 2001, yet fewer than 30% of those eligible are covered. With unemployment at 19%, many workers are no longer able to make contributions. On the other hand, former congressmen get 20 times more than the basic pension. The government has set up a new working-group, involving business and unions, to discuss reform. Even so, progress will be slow.

Juan Manuel Santos, the finance minister, is sticking to his forecast for economic growth of 3.8% this year and 4.5% next. He points to evidence that construction is picking up again after a long slump, and to a surge in imports of machinery. But after a slow first quarter, others reckon growth this year could be as low as 2.5%. That would make the fiscal target harder to reach. Given Colombia's problems, the IMF is likely to be accommodating.

Not so Colombia's politicians. This week, after three years of discussions, the Senate finally killed Mr Pastrana's plan for political reform, originally intended to encourage Colombia's guerrillas to make peace. The proposed reform would have required each political party to present a single list of candidates, rather than the current plethora. Proponents argue that this would have created stronger parties and reduced corruption. Politicians saw it as a threat to their hopes of re-election.

Mr Pastrana still has 14 months of his term left, but already attention is shifting to next year's presidential election. With Congress in no mood for radical measures, the prospects for reform are dimming.

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Kashmir

India decides to try talks

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India ends its ceasefire, but calls for talks with Pakistan's leader

IT IS an odd sort of peace initiative that begins with the cancellation of a truce. Yet India's decision on May 23rd to end its six-month unilateral ceasefire against the militants fighting its rule in Kashmir while inviting Pakistan's military ruler for talks could be the best news the region has had in a while. Talks between India's government and the Kashmiri separatists had been going nowhere, partly because Pakistan did not want them to. Enlisting Pakistan to seek peace was the only other option. For the first time since declaring themselves to be nuclear powers, India and Pakistan may be about to discuss their differences seriously.

Reuters

India's reversal of policy is dramatic. Its prime minister, Atal Behari Vajpayee, had initiated civilities in February 1999 when he took a bus from Delhi to Lahore, capital of Pakistani Punjab, and embraced his Pakistani counterpart of the day, Nawaz Sharif. The two promised in the Lahore Declaration to resolve their differences peacefully. A few months later India cried betrayal: it discovered that Pakistani troops had seized territory near the town of Kargil on its side of the "line of control", which divides Kashmir into zones controlled by Pakistan and India.

In the mini-war that followed, India ejected Pakistan from its part of Kashmir. It has since refused to talk directly to Pakistan as long as it backed militancy in the state. In October 1999 Pakistan's army chief, Pervez Musharraf, ousted Mr Sharif in a coup. Since India regarded General Musharraf as the mastermind of the invasion, this deepened India's resolve.

Instead, Mr Vajpayee tried to make peace directly with disgruntled Kashmiris, in the hope that Pakistan could eventually be persuaded to accept the deal. The unilateral ceasefire began promisingly in November, with Pakistan reciprocating by pulling troops back from the line of control. But India failed to tempt the All-Party Hurriyat Conference, the main political grouping of separatists, into talks. Militancy continued unabated and Kashmiris accused Indian security forces of unrelenting brutality.

With few people mourning the expired ceasefire, Mr Vajpayee is trying to de-emphasise the role of the separatists and move Pakistan to centre stage. He may not have forgiven or forgotten Kargil, but he has decided to finesse it.

For General Musharraf, Mr Vajpayee's invitation is a triumph. He had long been lobbying for talks, and seemed to regard India's rebuff as an insult to both Pakistan and the legitimacy of his government. Pakistan's standing in the West seemed to reach a new low earlier this month, when the American deputy secretary of state, on a visit to India, came close to calling it a rogue state. Mr Vajpayee's invitation has promoted General Musharraf from pariah to potential participant.

The new initiative could progress further than the last one, if only because, presumably, Pakistan will not stupidly repeat its prank of seizing Indian-controlled territory while pretending to talk peace. But it is not clear yet whether either side is prepared to concede enough to make it more than a temporary respite.

India will repeat its demand that General Musharraf should do what he can to stop “cross-border terrorism”. But at least it does not seem to expect that all violence will end immediately. A spokesman for India’s foreign ministry says that India has “decided to address the issue of terrorism through the security forces”, implying that low-level fighting will go on. Six Muslim militants were shot by Indian forces the day after the ceasefire ended. But an end to violence is no longer a precondition of dialogue but an objective of it. This suggests that General Musharraf will have at least a little time to deal with the anti-Indian militant groups based in Pakistan, which are the most implacable foes of compromise. One, Lashkar-e-Taiba, has reportedly dismissed India’s invitation as a “gimmick”.

But General Musharraf will pay a price for India’s relenting. Mr Vajpayee has in effect turned the clock back to February 1999, when Kashmir was just one of several subjects on a broader agenda for improving Indo-Pakistani relations. General Musharraf may now have to accept what he seemed to reject two years ago: negotiations that do not hold relations with India hostage to developments in Kashmir. This would be good news for the region. Kashmir is by far the most intractable dispute between the two countries, but nuclear confrontation is the gravest danger.

It is not clear whether talks will work in practice. India’s resumption of offensive operations against militant groups in Kashmir risks making a bad human-rights situation worse, despite the foreign ministry’s promise that its security forces would take “maximum care” to shield civilians from harassment. Mirwaiz Umar Farooq, a Hurriyat leader, claims that they have killed 13 people in custody in the past week, while the ceasefire was still nominally in effect. India’s offer of talks to “all sections” in Kashmir remains open. But the separatists will now take their cue from Pakistan.

Mr Vajpayee’s invitation to General Musharraf has given Pakistan some of what it wants, but it may not be enough. India’s formal position remains that Kashmir (including the Pakistan-controlled part) is an integral part of its territory, though most observers think it might agree to divide the state along the line of control. India’s notion of dialogue on Kashmir is discussing ways to reduce militancy, whereas Pakistan champions “self-determination” for the Kashmiris, in other words Kashmir’s accession to Pakistan. Peace requires a quick compromise between these seemingly irreconcilable positions or, more likely, a productive delay.

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Pakistan

Quick march to power

May 24th 2001 | LAHORE
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General Pervez Musharraf aims to stay in charge

THERE is no longer much doubt about it. General Pervez Musharraf, the army chief, means to become the next president of Pakistan, and a powerful one. He has implied as much in private gatherings. The finance minister, Shaukat Aziz, has been quietly assuring the IMF and the World Bank that the general will remain in charge even after next year's promised general election to "ensure continuity in the economic-reform package" currently being delivered. The government has created the post of deputy chief of army staff for General Muzaffar Usmani, a close confidant of General Musharraf's. The deputy will run the army while his boss gets on with ruling the country.

It is thought that General Musharraf may make an announcement after the third and last batch of local elections in August and before his term as head of the army expires on October 7th. He is expected to extend his tenure in that role by at least one year. Then the constitution may be amended to change both the election of the president and his powers. At present the president is elected by members of the national and provincial parliaments, who barely number 700. Under the new arrangements the president is expected to be elected by nearly 250,000 "non-party, grassroots democrats" on local councils.

The president's job is largely ceremonial at present. But General Musharraf plans to sit atop a mighty National Security Council comprising the service chiefs, the prime minister and some members of the cabinet. The president will have the power to hire and fire the service chiefs as well as the prime minister and national and provincial parliaments. The Supreme Court has ruled that the general may amend the constitution, provided he does not change the parliamentary and federal system of government or tinker with the independence of the judiciary.

If there are any obstacles to his ascent to legitimated power, General Musharraf does not seem to expect them. "The politicians are all useless and have no credibility," he says. But Benazir Bhutto and Nawaz Sharif, both former prime ministers now in exile, still command the loyalty of most voters in the country. Their parties are represented in a group called the Alliance for the Restoration of Democracy. This week the Alliance said it intended to defy a ban on political rallies and arrange pro-democracy "events" in the western city of Quetta on June 7th and 8th. Attempts to stage rallies in Lahore in March and in Karachi this month were thwarted by the security forces.

General Musharraf claims that Pakistan is "on the road to economic recovery". Helpful countries have rescheduled some pressing debts and the IMF has approved a couple of hundred million dollars in loans. But the GDP growth target has been lowered from 4.5% to 3.8% this year. The European Union remains highly critical of the military dictatorship. The United States has moved perceptibly closer to Pakistan's arch-enemy, India. "Our defence is impregnable," the general boasts frequently, as the Indian army continues to fence the border in Kashmir and holds threatening military exercises along its frontier with southern Pakistan.

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Singapore

No laughing matter

May 24th 2001 | SINGAPORE
From The Economist print edition

Despite talk of an opening-up, politics on the island remains a one-sided affair

Free speech, Singapore-style

"REINVENTING politics", reads the slogan on name-cards handed out by members of Think Centre, a tiny Singaporean pressure-group. It is a bold notion: since independence, Singapore's rulers have been so secure in office that the only aspect of politics in need of reinvention has been the opposition, whose leading lights have trodden a forlorn path of defamation suits, criminal prosecution and emigration. But in recent years even Goh Chok Tong, the prime minister, has been talking of the need for "a new vision for Singapore, an ideal, a fresh mindset". Are refreshing breezes wafting through the political climate?

Not really: sitting so close to the equator, Singapore does not have anything as dramatic as the season temperate countries call "spring". Yet there are subtle variations of temperature, and a number of initiatives suggest a warming-up: last September, in Hong Lim park in central Singapore, a "Speakers' Corner" opened. Think Centre itself has made quite a splash, as has a non-partisan political-discussion group, the Roundtable; and the Internet has opened up free-wheeling debate and even, on talkingcock.com, a site devoted to Singapore, political satire.

"All a show," says J.B. Jeyaretnam, a nominated MP, who constitutes a third of the opposition: the ruling People's Action Party (PAP) won 81 out of the 83 elected seats in the last election, in 1997. Mr Jeyaretnam's bitterness is understandable. He has been declared bankrupt for failing to meet payments of damages awarded in defamation suits (not, on this occasion, brought by members of the cabinet). If an appeal to be heard in July fails, he will lose his parliamentary seat and be disqualified from the next election, expected later this year or early next. One of Think Centre's recent reinventions was to help organise a "Save JBJ" fund-raising rally. It produced some S$19,000 ($10,000), towards the S$235,000 needed.

Already, in December, Think Centre had arranged an event at Speakers' Corner, to mark international human-rights day. That provoked a police investigation and a warning, since it smacked of an organised demonstration. When it first opened, Speakers' Corner attracted hundreds of visitors. It now keeps going largely thanks to one stalwart speaker, Tan Kim Chuang, a stockbroker, with a loyal audience of a dozen or so middle-aged and elderly men. Mr Tan has already spoken more than 50 times and, one day this month, was one of just three names on the list, posted at the conveniently adjacent Kreta Ayer Neighbourhood Police Post, of those registered in advance to speak.

Like so much else in Singapore, Speakers' Corner is based on an idea by Lee Kuan Yew, the senior minister, and comes with restrictions. The topics of race and religion are out of bounds, speakers must register and no amplification is allowed—prompting talkingcock.com to joke that now Singaporeans have the right to speak, they need the right to hear.

Nevertheless, Singapore is a more relaxed and open place than it was, both socially and, despite strict censorship, culturally. Simon Tay, an unaffiliated nominated member of parliament, detects "a sense of tentative change, and of government seeking to manage social change". But, politically, the dominance of the PAP is as secure as ever. Partly that is a result of its success. With GDP per head higher than Britain's, Singapore is a safe, modern, high-rent enclave in an increasingly dodgy neighbourhood. Why fool around with opposition politics?

The passage last year of a law on political-party finance has made the opposition's life even harder. It bans foreign funds and anonymous donations by Singaporeans of more than S$5,000 in any one year. And the government carefully polices those it believes may meddle in domestic politics, such as the

foreign media. Last month it amended its broadcasting legislation to make it clear that satellite-television news stations were subject to the same rules that apply to the foreign press, in whose pages the government demands a right of reply—see, no doubt, next week's issue of *The Economist*.

Think Centre itself, along with another group, the Open Singapore Centre, chaired by Mr Jeyaretnam, were both named in March as "political associations", subject to the political-donations law. In response, Think Centre announced it would field candidates at the next election. This, it later revealed, was an April Fool's Day joke. It did not go down well. In Singapore, politics is no laughing matter.

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Afghanistan and Iran

The odd couple

May 24th 2001 | HERAT
From The Economist print edition

The Taliban's useful neighbour

THE government of Iran has the most tentative of relationships with the Taliban, who rule most of Afghanistan. Like nearly all other countries, Iran does not formally recognise the Taliban as the government of Afghanistan, but it is allowed to maintain a consulate at Herat in the west of the country. This week the consulate was empty. Part of it had been ransacked earlier this month when a mob attacked the building. Nonetheless, both countries are expecting the consulate to be functioning again soon.

The advantage for the Taliban is that Iran is fairly relaxed about its border with Afghanistan, despite the UN sanctions that have stopped most of the Afghans' external trade. Shops in Herat are full of Iranian products. Every day well-filled lorries make the journey to Herat from the Afghan border town of Islam Qila. The advantage for Iran is that it can keep on good terms with a worrying neighbour. One day it may help Afghanistan to be reconciled with the outside world.

The attack on the Iranian consulate on May 4th followed a bomb explosion in Herat that killed ten people. The mob believed that the Iranians, who are Shia Muslims, were responsible. The Taliban and their supporters are Sunnis. One of the dead in the bomb attack was a Sunni Iranian in exile in Herat. The Taliban said the consulate staff were not to blame, and escorted them safely to the border. It is believed that the Taliban's governor of Herat hid the consulate's staff in his back yard. A Taliban spokesman said, however, that Iranians opposed to ties between the two countries had set off the bomb. In 1998, 11 Iranians, among them nine diplomats, died when the Taliban captured the town of Mazar-I-Sharif from opposition forces led by Ahmad Shah Masoud.

Iran has supported Mr Masoud in the past, and has given sanctuary to some members of the government deposed by the Taliban. It still keeps lines open to the opposition. With the Taliban and Mr Masoud's forces warming up for a summer clash, Iran will be wanting to return as soon as possible to its observation post in Herat. Will the coming battle be the end of Mr Masoud, or will the Taliban once again be deprived of their goal to be the rulers of all Afghanistan? Iran is likely to be among the first to know.

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Australia's budget

Bribery time

May 24th 2001 | CANBERRA
From The Economist print edition

The government bids to stay in power

AFTER five years in power, and with an election looming this year, Australia's conservative coalition government led by John Howard is looking decidedly shaky. Fissures opened up in its ranks a few weeks ago when an explosive document, written by a top official in the Liberal Party, which Mr Howard leads, was leaked to the media. It described the government as "mean, tricky and out of touch", unintentionally giving the opposition Labor Party a raft of ready-made slogans for the coming campaign.

When Peter Costello, the finance minister, presented the last budget of the government's term to Parliament on May 22nd, he was faced with a choice: to continue the coalition's steady run of mounting surpluses, bolstering its claim to be a more responsible economic manager than Labor, or to raid the coffers in a bid to buy its way back to power. Not surprisingly, he chose the latter.

The government has never really recovered politically from the introduction a year ago of a new tax system, whose centrepiece was a tax on most goods and services in exchange for lower income and corporation taxes. The reforms were overdue, but the government bungled the way some aspects of the system were introduced. Small businesses complained about the high costs of complying with it. Elderly Australians on fixed incomes felt left out of the prosperity being enjoyed by younger wage-earners.

Both disaffected groups have tended to support the Liberal Party, and many of their members live in marginal constituencies along the urbanised east coast, where Labor needs to snatch only a handful of seats to take power. Throw in farmers and town-dwellers who have turned against the National Party, the coalition's junior partner, whose power-base lies in regional Australia, and the government has had to concentrate on survival at all costs.

The main cost has been its reputation as a market-driven, low-spending administration that produced fat surpluses. In this week's budget, the surplus was whittled down to just A$1.5 billion ($780m). Spending on new measures rose to almost A$4 billion. A big chunk of this went towards trying to win back the grey vote by compensating older Australians for their higher living costs under the new tax system. It offered more than 2m cash payments of A$300 each before the financial year ends in June, and income-tax breaks likewise designed to take effect in the current financial year. The budget also committed more money to help the owners of small businesses to buy cars, the unemployed to find jobs and people in the countryside to get health care. With the negligible surplus, Mr Costello has left the Labor leader, Kim Beazley, little room to offer big promises in the election. There has even been talk that, if voters like the budget, Mr Howard will call a snap election around July instead of waiting until November, as he has said he would. But this would be a gamble. Mr Howard would not want to risk missing a planned visit to Washington to offer personal support for President George Bush's missile-defence plans, or playing host to a meeting of Commonwealth leaders due in Brisbane in October. When it comes to election timing, ego may trump opportunism.

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Indonesia

Burning books

May 24th 2001 | JAKARTA
From The Economist print edition

What lies behind Indonesia's anti-communist surge?

A SPECTRE has long haunted Indonesia: anti-communism. But its recent re-emergence is arousing puzzlement as well as fear. Spontaneity is a rare commodity in Indonesian politics, where even seemingly random events are believed to be "engineered". So it has been with the formation in April of an "anti-communist alliance" (AKA) of more than 30 right-wing and Muslim groups. Its activities in recent weeks in Jakarta and other cities have included purges of bookshops' shelves, burning of suspect books and attacks on left-wing politicians and their offices. On May 20th alliance supporters marked one of the anniversaries of Indonesia's nationalist movement with a menacing "sweep" of Jakarta's bookshops.

Hundreds of thousands of Indonesians died in the killings of alleged communist sympathisers that accompanied the rise to power in 1965-66 of Suharto, whose dictatorship endured until 1998. At the time, the Indonesian communist party, the PKI, was the world's third-largest after the Soviet and Chinese parties. But it has been proscribed ever since, and has seemed a spent political force. That did not stop the Suharto regime using it from time to time as a pretext for a bout of repression; and many Indonesians still believe that the creed retains some secret loyalists.

The chairman of the AKA is Eurico Guterres, who sprang to fame as the leader of one of the most vicious of the government-backed militias that did their best to destroy East Timor after it voted for independence in 1999. Guterres was convicted of weapons offences and is now serving a comfortable six months of house arrest. His background makes it seem unlikely that the AKA is his own idea.

The alliance suffers from a lack of obvious books to burn. So it has tried to suppress a critical book on Karl Marx by a Roman Catholic priest; the works of Pramoedya Ananta Toer, Indonesia's most famous novelist; "The Prophet" and other books by Kahlil Gibran, a Lebanese poet; and "Chicken Soup for the Soul", a self-help best-seller. Bookshop-owners have been alarmingly quick to purge their shelves, showing that the self-preservation instincts bred under President Suharto still linger.

Among the human targets is Budiman Sudjatmiko, the leader of the PRD, a small left-wing party. He was jailed in 1996 and was among the political prisoners freed when Abdurrahman Wahid became president. Mr Budiman sees the AKA as an alliance between opponents of democratic change: these include members of Golkar, the ruling party under Mr Suharto, and some of the more radical Muslim groups.

More detached observers broadly agree with this analysis. The movement seems designed both to weaken the president, who has called for the lifting of the ban on communism, and to besmirch the motives of those calling for faster and more radical democratic change. By the same token, it strengthens the party led by Megawati Sukarnoputri, the vice-president, or at least of those elements in it with deep roots in the old regime, such as Mr Guterres himself, and some retired generals. Like many other events where the suspicious detect "engineering"—such as the bombings last Christmas of Christian churches, or ethnic violence in the Moluccas and Borneo—the new anti-communism creates a climate of instability and, perhaps, a hankering for old dictatorial certainties.

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The EU's regional aid

What's ours is ours

May 24th 2001 | BRUSSELS
From The Economist print edition

What should happen to the EU's aid to its existing poor regions when East European countries with far poorer ones join its ranks? The EU is split

Get article background

EPA

A NEW motorway under the Spanish town of Malaga; the modernisation of the Belgian port of Zeebrugge; a restored medieval abbey in Ireland; a drop-in centre for drug addicts in Lisbon; training programmes for unemployed southern Italians. All these examples of the largesse of the European Union were displayed this week in glossy brochures and at promotional stands as European leaders met in Brussels to discuss the future of the EU's regional aid policies.

But the tone of the gathering was anything but celebratory. A row has broken out over the future of regional aid, which will consume *euro*213 billion (say, $180 billion), around 35% of the EU's budget, between 2000 and 2006. The trouble springs from the prospect of "enlargement": the spread of the EU to take in up to 12 new countries, mainly in Central and Eastern Europe. The prospective new members are poorer than the existing 15. Under EU rules, a region's GDP must be 75% or less of the EU average to qualify it for "structural" funds, the bulk—*euro*182 billion—of that *euro*213 billion total. Apply these rules in an enlarged EU, and the juiciest subsidies will flow to regions of countries like Poland and Hungary, rather than, as now, Spain, Greece and Portugal.

The Spanish can see that the fiesta may soon be over, and they do not like it. The government of Jose Maria Aznar has issued a paper claiming that its own poorer regions will be the victims of a "statistical illusion" in an enlarged EU. They will not be any richer, but eight of the 11 (out of 17) Spanish regions that get EU aid at present will no longer fall below the 75% threshold, and so will be ineligible for aid. That, say the Spanish, is unacceptable.

Rather curiously, they are invoking the vaunted principle of EU solidarity to demand that the subsidies keep flowing. A normal interpretation of that word might suggest that it would be time for Spain, having benefited from EU generosity, to be generous in turn. But Mr Aznar is under political pressure at home. The money is big, and besides, it is part of Spanish political folklore that Felipe Gonzalez, the former Socialist prime minister, successfully fought off German attempts to cut subsidies to Spain in the early 1990s. Mr Aznar cannot be seen to do worse.

Spain leads the efforts to protect the financial privileges of the current recipients of regional aid, but it is not alone. Portugal and Greece, other notable beneficiaries, are urging the Spanish on. Ireland, whose GDP per person is now well above the EU average, knows that the game is up. But Italy, once Silvio Berlusconi is in the saddle, can be expected to weigh in (see article). Its poor south—and those who run it—also does well from the system.

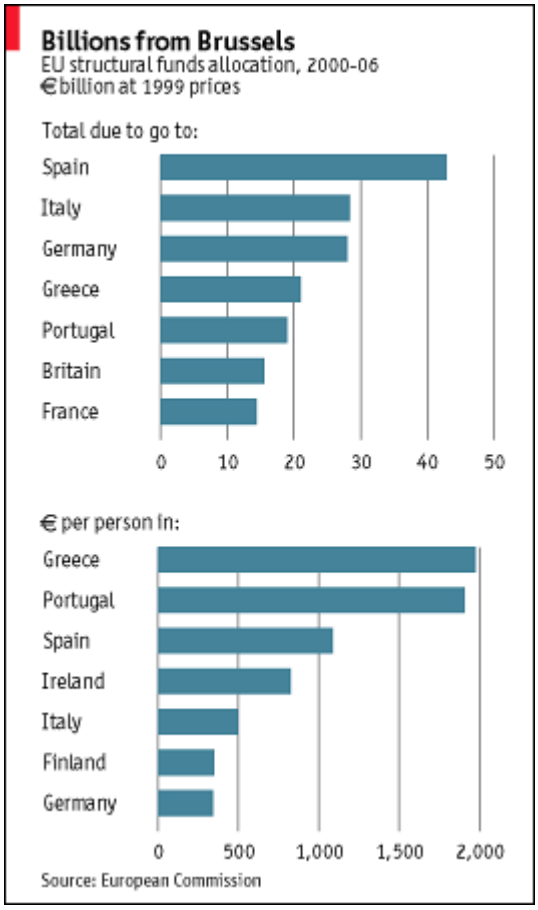
Ways out?

All this poses a problem. To negotiate with the applicants, the EU needs to make up its mind about the future of its big spending programmes, those for regional aid and agriculture. But Spain is threatening that, if it does not get some guarantees on regional aid, it will block internal EU agreement not only on that but on other sensitive topics, such as the free movement of labour. Hans Eichel, finance minister of Germany—which has its own axes to grind on free movement—has called this "blackmail".

The European Commission is already floating some ideas for

buying off the Spanish and the others. Though their structural aid will be reduced, it will not be cut off at one blow. Some still more expensive ideas are in the air. One is to raise the threshold for eligibility for structural funds to 90% of the EU's average GDP. Another is to use unemployment—still high in Spain—rather than relative wealth as a basis for calculating eligibility. The EU has already proved adept at inventing such politically inspired fudges on aid. Even under current rules the Union has managed to ensure that every country, no matter how rich, gets some sort of structural aid.

Any compromise is bound to be expensive. One thing the Poles and the Spanish do agree on is that it would be a great idea to breach the current limit on total regional aid, which is capped at 0.45% of the EU's GDP. A study circulating at this week's conference suggested 0.66%, which means an extra *euro*20 billion a year. The big contributors to the budget, notably Germany, would not wear that. Indeed a policy paper issued by the ruling German Social Democratic Party suggested returning regional aid largely to national control.



Does it work?

Lost in this squabbling is the question of whether regional aid works. The European Commission says yes, noting that over the past decade income per person in Spain, Greece and Portugal has risen from 68% to 79% of the EU average; and that poor regions too have generally been rising toward it. But a new study by two European academics, Michele Boldrin and Fabio Canova, casts doubt on this rosy picture. EU aid to poor regions, they say, "does not appear to enhance the capacity of these regions." It is not so much development aid, they say, as mere income distribution.

The fact that Greece, Spain and Portugal are catching up does not prove the case for structural help, they argue: any poor country will tend to catch up once it joins a free-trade area with richer ones. And its poor regions will share in the trend. The most significant figure, say the two academics, is the gap between rich and poor regions within a country—and in most of the countries whose poorest regions have been big recipients of EU aid, that gap has widened over the past decade, especially in Spain, Greece, Italy and Britain.

Of course defenders of regional aid can argue that things would be even worse without the EU's largesse. And ordinary voters do not read academic papers. But the row may cause some in rich countries to ask the awkward questions buried in talk of solidarity. Do they feel it? Just why should the citizens of Bristol or Brussels pay for a road to Bialystok or the new airport building, shown on the, of (none-too-poor) Bilbao?

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Italy and the EU

Questions, at last

May 24th 2001 | MILAN
From The Economist print edition

For the first time, an Italian government may not offer uncritical devotion

AFTER decades of unquestioning support from Italy for the European Union, its new government may take a new line. Within days of Silvio Berlusconi's victory, Giulio Tremonti, his likely finance minister raised doubts about enlarging the EU: not too fast, he said, the development of Italy's south must come first.

From the European Commission came cries of horror. Romano Prodi, in 1996-98 a centre-left prime minister in Italy, averred that there was no link between enlargement and EU aid to poor regions. Mario Monti, the competition commissioner, declared enlargement "an absolute priority".

AP

Corleone has a Brussels godfather

This sort of debate is novel to Italians. They like the EU. When they had to cough up a special tax to qualify for the future euro-zone, they paid without moaning. Today 61% of them trust the European Commission; the EU average is 46%. During the election campaign, the issue did not arise. So why did Mr Tremonti say what he did?

Because that's what he thinks. The centre-right's few eggheads have a practical, unromantic approach to the EU. Antonio Martino, briefly foreign minister during Mr Berlusconi's short prime ministership in 1994, denies he is a Eurosceptic, but he talks like one. He also likes America, and its current administration, a lot. With Mr Tremonti, he and a few others will shape Italy's future European policy. And Mr Berlusconi's best friend abroad is Spain's Jose Maria Aznar, whose enthusiasm for enlargement is yet to be proven.

Policy will depend much on who becomes foreign minister. There are two candidates left: Pier Ferdinando Casini, leader of the Christian Democratic Centre, a staunch ally of Mr Berlusconi; and Renato Ruggiero, a former head of the World Trade Organisation, and before that a diplomat and Fiat's ambassador-at-large.

Mr Casini, aged 45, has little international experience. He would probably be closer to his boss, and to Mr Berlusconi's foreign-policy mentors. In contrast, Mr Ruggiero, at 71 a tough and experienced negotiator, is a firm pro-European. He is said to have told Mr Berlusconi that he would not take the job unless he could carry on that Italian tradition—and act as a foreign-affairs professional, not a political pal.

Mr Berlusconi once said he wanted a politician, and his main political allies certainly would. But he may have had second thoughts: a respected international figure like Mr Ruggiero might improve his own image abroad. And President Carlo Azeglio Ciampi is watching the race closely. He too is a keen European.

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Charlemagne

UEFA's Gerhard Aigner

May 24th 2001
From The Economist print edition

Keeping order in European football is quite a business

THE man handing out the medals under the stadium lights is the official face of European football: Lennart Johansson, the Swedish president of UEFA, its governing body. But the figure in the background handing them to him is no gofer: he is Gerhard Aigner, UEFA's German chief executive. The two together make a strong team. And they are not here in Milan, at the final of UEFA's annual Champions League, for the champagne.

Football—association football, in full, hence "soccer" to English public schoolboys a century ago and to Americans today—is Europe's number-one sport, both a weekend kickabout for millions of amateurs and big business too. And as a business, an odd one. Its main, but very mixed, components, the league clubs, tend to be owned and run, hands-on, by tycoons, mostly egocentric, many eccentric (who else would want the hassle and the cost?), one or two criminal. The clubs are grouped into national cartels. Many are local monopolies. They fire managers the way Elizabeth Taylor gets through husbands. Yet many lose money. Their overpaid but often unhappy workforce is also their main asset—but one that at any moment may cease to function, and whose capital value can crash alike at the break of a leg or the ruling of some sports-blind Eurocrat or court.

Goodbye to amateurism

This is the multinational flux of interests, egos and umpteen-figure finance over which UEFA has to rule; UEFA, which itself owns little but its moral authority, a glass and marble palace on the edge of Lake Geneva, and the rights to sundry competitions. And this while dickering with the outside paymaster, television, and fighting off antitrust zealots in Brussels. For UEFA, like any monarchy, a high profile and public accceptance are essential.

That was not always so. UEFA was born in 1954, when top-level football had long been a professional game but its regulation was not. When Mr Aigner, a keen amateur player and later referee, joined it in 1969, its shabby offices held only a handful of staff. Even in 1989, when he became general secretary—the title says a lot—they totalled only 30-odd, though the Klondike of television cash was already transforming football. Then UEFA struck lucky, twice: Mr Johansson in 1990 became its president, and in 1998 failed to do so at FIFA, the game's world body. That year, belatedly, UEFA called in consultants, to help reshape it for the newly rich and complex world of European football. With its ancient network of elected committees, "we were drowning in paper," says Mr Aigner. "We couldn't fix priorities. Now we've become a business." Hence his new CEO title, and a board of executive directors to speed up day-to-day decisions. Hence too a communications chief hardened in the rough world of British political spin-medicine. That's just as well, for big as the money is these days, so, not by chance, are the issues.

Football money and football power

UEFA runs 13 competitions. Three are gold mines: the four-yearly international European championship; the annual Champions League, for clubs; and the UEFA Cup, less prestigious and less profitable. The latest Champions League has earned, mainly from television, some SwFr1,000m ($570m), not counting ticket money, which the clubs keep. Of that, 72% is shared by the 32 qualifying clubs, on a formula reflecting how well each did and how many televiewers it attracted. The result last year ranged from SwFr5.3m to SwFr44.9m for the winners, Real Madrid.

Those sums illustrate European football's biggest problem. Its real masters are not UEFA, not the 51 national associations that are its members, not the national leagues nor yet the mass of clubs, but a few rich clubs; and the gap between these and the rest is widening, as money buys the best players, which

brings success and more money. America has solutions: the draft system (the worst teams get first pick of new players), team salary caps and, in American football, revenue-sharing. UEFA has no such tools. It talks of salary caps. Some clubs would be happy, Mr Aigner says, but admits it would be hard to police the figures.

He blames much of the trouble on the 1995 “Bosman decision”. In it, the European Court decided (i) that a Belgian player of that name had the right, being out of contract, to join a French club though his old one would get no fee; and (ii) that rules limiting the number of foreigners in a club squad broke EU law on free cross-frontier movement of labour. Point (ii) freed rich clubs to buy players from all over the EU. By now, even rules limiting non-EU players are being relaxed—indeed in Italy this month abolished entirely. Point (i) also has been extended, to Mr Aigner’s woe: it inspired the European Commission to denounce all transfer fees, be the player in contract or out, as restraints on movement. A blow against the moneybags? No. They would still rule, buying stars with huge wages instead of huge fees, which do or may at least go to the small clubs that trained them.

The transfer-fee battle was almost lost, when FIFA—whose business, in theory, it was—first flounced, then floundered, then put up the white flag. UEFA and European clubs, with real business at stake, rushed to pull it down. Lobbying of governments won a decision at the EU’s Nice summit last December that sport is a special case. The commission retreated into a compromise, though the working-out of its details still has UEFA on edge.

The affair spoke well of UEFA’s zeal to keep close to the real forces of football (a lesson FIFA would do well to learn). Yet it carried a warning too: the clubs have clout. Mr Aigner still hopes for a limit on a club’s foreigners; they do not. He wants fewer clubs in the Champions League; less money for us, they say. UEFA in 1998 saw off a scheme for a super-league of Europe’s big clubs. For how long? Fourteen are already formally grouped, with an office in Brussels. Though UEFA plans a club-licensing system (no licence, no UEFA competitions), in the end, as Mr Aigner accepts, “we rule by consent.” Will it always be there?

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German diplomacy

Plain speaking, plain cover-up

May 24th 2001 | BERLIN
From The Economist print edition

The leak of an ambassador's cable is causing red faces and rage

WRITING a frank report, as Jürgen Chrobog, Germany's man in Washington, did, is an ambassador's work. Leaking it is a fool's. Or a knave's? Mr Chrobog's account of a meeting on March 29th between President George Bush and Chancellor Gerhard Schröder was full of more-than-frank comments by their aides. Made public, it has enraged Muammar Qaddafi and Yasser Arafat, alarmed Vladimir Putin and, worst, strained Germany's relations with the United States.

AP

Lockerbie: a Libyan bomb did it

The meeting included Mr Bush's secretary of state, Colin Powell, his national security adviser, Condoleezza Rice, and Mr Schröder's top diplomatic adviser, Michael Steiner. According to the ambassador's leaked report, Mr Steiner, recounting talks earlier in the month with Colonel Qaddafi, said that the Libyan leader had "admitted that Libya took part in terrorist actions (La Belle, Lockerbie). He clarified that he had abandoned terrorism and seeks the opportunity to make Libya's new position known." For La Belle, read a night-club bombing in Berlin in 1986 that killed three people and wounded over 200; for Lockerbie, the bomb that brought down a PanAm jet in Scotland in 1988, killing 270.

Explosive stuff. Not quite that explosive, says the German government: the colonel indeed admitted to terrorism in general, but no specific cases were mentioned; the two named were Mr Chrobog's gloss.

Mr Powell is reported as describing Mr Arafat as having "lost touch with reality", Mr Steiner as calling Jordan's King Abdullah "one of the most intelligent leaders in the region, and also one of the most powerless". So be it, one might say. That was not what the Russians said to the report that Mr Schröder had argued for no more foreign aid to be sent to Russia until it stopped the capital flight that carries the cash promptly out again to bank accounts abroad. "A provocation aimed at destroying the positive trend in relations between Russia and the European Union," was Mr Putin's angry comment on the leak, saying he did not believe it was authentic. Many others, whether or not wishfully, do.

The Americans and the Germans are now desperately trying to play down the incident. But it is a huge embarrassment for Mr Schröder—an example of "how disreputably and unprofessionally the government conducts its business", crowed the opposition Christian Democrats. Mr Steiner, already summoned to testify in the trial of five Libyans for the La Belle bombing, will probably have to appear before a Bundestag committee too.

How and why did the cable get to the media? After reaching the foreign ministry, it was sent to Mr Steiner in the chancellery for editing and approval—and then given one of the lowest security classifications, "confidential: for internal use only", and circulated widely within the bureaucracy. And so, inevitably, outside it.

So far, so foolish, at least. But was there worse? Rivalry between the chancellery and foreign ministry over foreign policy is traditional. But there are extra motives today. As Mr Schröder has shown an increasing penchant for diplomacy, so tensions with his Green foreign minister, Joschka Fischer, have grown. Mr Fischer was especially miffed when Mr Schröder ousted him from the limelight in the debate over the future of the EU, for example. And a general election is due next year.

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France's public sector

They love it

May 24th 2001 | PARIS
From The Economist print edition

Most Europeans have gained from privatisation, and most believe in market forces. France's rulers and citizens alike believe in neither

"WE MUST not abandon public service to economic liberalism: Britain's railways and America's airlines are not examples to follow." Ah, no: the TGV high-speed trains are comfortable, punctual and cheap, and Air France still serves wine without charging extra. So if François Loncle, a Socialist member of the French parliament, does not speak for all his compatriots, he certainly speaks for most. Hence the government's stubborn refusal to open France's energy industry to real competition, despite pressure from other European Union countries and the European Commission. With presidential and parliamentary elections due next year, politicians have more to gain by defending France's public sector than decrying it.

EPA

Great train, great viaduct, great bill for the taxpayers

Why, when voters in most other countries associate the public sector with poor service and inefficiency? One reason is that a lot of French voters are part of that public sector. Central- and local-government civil servants; police; hospital workers; teachers; post and telecoms workers; electricity and gas workers; the armed services—together they add up to some 6m people, a quarter of the workforce, as against 13% in Germany and Britain.

But bigger reasons lie in France's history and culture. The idea of a beneficent state controlling the economy has been around since the 17th century, when Louis XIV and his dirigiste finance minister, Jean-Baptiste Colbert, nationalised the tobacco industry. In the 19th century public money helped entrepreneurs build railways, set up banks and dig coal mines. In the 1930s the Popular Front government of Léon Blum made itself popular not just by cutting the working week and guaranteeing annual holidays for all but by nationalising (with dire results for productivity) the defence and aircraft industries, the railways and the Bank of France.

In the second world war, French industry tarnished itself by collaboration with the Nazis. Come 1945, it was logical for the state, besides setting up its own oil company, to nationalise the electricity and gas companies, the Renault car company, the insurance companies and the banks.

What followed was what the French love to call *les trente glorieuses*, the 30 glorious years in which the birth rate, the economy and living standards all boomed in unison. Indeed, the public still laud Electricité de France (EDF) and Gaz de France (GDF) for restoring the nation's light and heat in the war's aftermath—a reputation that helped mute the criticism of EDF at the end of 1999 when hurricanes left much of France in prolonged darkness. When François Mitterrand brought the left back to power in 1981, it was with a mandate not, like Margaret Thatcher in 1979, to roll back the frontiers of the state but to extend them. He nationalised 36 banks and the leading companies in chemicals, glass, aluminium, electronics and armaments. Almost at a stroke, the state's share of industrial output rose from 15% to 30%.

There was, of course, an initial cost to the taxpayer—and there is a continuing one. EDF and GDF make lots of money. Even the post office has been in profit for four years running. But other state companies have gobbled subsidies. The disastrous performance under state ownership of the Crédit Lyonnais bank will eventually have cost taxpayers some FFr120 billion ($16 billion). Meanwhile, the price they pay for France's superb rail network will this year be a loss for SNCF, the state-owned railway company, of over FFr1 billion francs—its fourth loss in five years.

Pressure, who cares?

Can it go on? To qualify to join the new euro-zone, successive governments have been under pressure to undo the nationalising follies of the early Mitterrand years. The current Socialist-led one of Lionel Jospin has been quite as active as its conservative predecessors in selling state holdings, for example allowing private capital into France Télécom and the aircraft builder Aérospatiale. And the European Commission can bite: it has gone to law over the protected positions of EDF and GDF, and increasingly it allows aid for state companies only with a pledge to privatise.

Yet, for all the pressures, the state's holdings remain enormous. It owns all of EDF, GDF, the post office, the rail system, the Paris airports, the nuclear industry, the aero-engine maker SNECMA; most of Air France, France Télécom and Thomson Multimedia; significant bits of Renault, the Bull computer company and—still—Crédit Lyonnais; and much more. In all, the state has a majority stake in some 1,500 companies and a minority in 1,300 others. So much for modern free-market capitalism.

Yet free-marketeers sneer in vain. Most French people see the market as a jungle, to be feared if it cannot first be tamed by the state. Only the tiny Liberal Democratic party of Alain Madelin is happy to let Adam Smith wave his invisible hand. And although France's public employees are a cosseted lot, many retiring at 55 or even earlier, enjoying generous pensions and ever ready to strike (the railway workers, 1% of the labour force, accounted for 40% of all time lost by strikes in 1998 and may do even worse this year), the rest of the citizenry is ever ready to indulge them.

Indeed, according to opinion pollsters, two-thirds of the nation believes the public services in general perform well—even the arrogant civil service, mandarin at the top and citizen-disdaining below. For France Télécom and the post office, the proportions rise to 92% and 80%. In sum, till the elections are over, who cares what the European Commission thinks?

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Central Europe's roads

Crash, bang, wait

May 24th 2001 | EN ROUTE TO BUCHAREST, MAYBE
From The Economist print edition

The roads in ex-communist Europe are still pot-holed, jammed and deadly

WHY should West Europeans pay to build roads in ex-communist, now would-be EU, countries to their east, did someone ask? He or she should try driving on them.

The road from Poland's Baltic port of Gdynia to Romania's capital, Bucharest, begins well enough. A nice jaunt round the harbour, an obedient stop at a new set of traffic lights, and in a flash you are on a new stretch of motorway. For Poland, this is exciting. Traffic moves speedily and smoothly, exits are clearly marked, hypermarkets gleam on either side. It seems too good to be true.

And so it is. Twenty minutes later, the motorway peters out, to become a crumbling little country road. Welcome back to the relentless jams of the old Central Europe, made far worse by a doubling in traffic since the end of communism.

The challenge of knitting together a half-way competitive transport network still overwhelms Central European governments, despite the efforts of the European Union to help. The EU's lofty if not very green ideal is to tie all of Europe together by a new web of motorways, or, in EU jargon, "transport corridors". The Union set up an agency in Vienna called the Transport Infrastructure Needs Assessment for Central and Eastern Europe. On its estimate—it has now shut up shop, its work done—to bring Central Europe's roads up to scratch by 2015 would cost $48 billion. Romania and Poland are in worst shape: Poland needs $16 billion, Romania $12 billion.

Most of Central Europe's arterial roads are clogged. In western Poland, the main east-west highway carries ten times as much traffic as in 1989. In Poland as a whole, the number of cars has risen by 70% in the past decade, while the number of rail passengers has fallen by half. Roughly the same pattern has emerged elsewhere, from the Baltic in the north to Bulgaria on the Black Sea. One trouble is the dearth of alternative routes. When a bridge in Poland, on the road linking Moscow to Berlin, was closed for repairs not long ago, the resultant traffic jam stretched across the entire country.

Such gridlocks are expensive. In EU countries, transport uses up about 4% of GDP, in Central Europe twice as much. And the roads are far more dangerous. Rare is the journey in Central Europe when you do not pass the relics of a grisly accident. Romania's death-rate per vehicle is nearly three times the EU average, Poland's double. Even the Czechs, with the safest roads in Central Europe, are twice as prone to lethal crashes as West Europeans.

One feature of a trip from the Baltic to south-eastern Europe is the variable state of the roads. One minute you are purring along a motorway, in Slovakia, for instance. Then the motorway stops dead, and you are back on a pitted track—a legacy, to some extent, of an ousted prime minister, Vladimir Meciar, who had roads built where he thought there were votes to be won, and not elsewhere.

Slovenia has done best of the ex-communist countries. Its motorways are so good that many drivers pass straight through the tiny country, from Austria to Croatia, barely noticing that they have been in it. "They don't even spend a cent," complains a Slovene minister. Once in Croatia, you are back in a jumble of pot-holes, jams and crashes. There, the main coast road is particularly slow and twisty. In Serbia, the old Highway of Brotherly Love, once the Balkans' main trade artery, has been torn up by NATO bombs. Many of the fancy cars with Italian and German licence plates on Serbian roads are stolen. "Come to Yugoslavia," a wry Serbian slogan has it. "Your car is waiting for you!" In Romania the road is slower still. In the north-west of the country, wooden wagons drawn by horses, often driven by Gypsies, far outnumber motor vehicles.

Across Central Europe at least one or two western features have arrived. Even in rural areas, smart petrol stations have sprung up. At a lonely one in Bosnia, at 2am, this correspondent was able to buy a

cappuccino—and *The Economist*.

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General election

The angry brigade

May 24th 2001 | BIRMINGHAM
From The Economist print edition

Some of the disaffected people who feel mainstream politics is passing them by could make their mark on the election

THERE is an unfortunate coincidence on June 7th—between polling day and the first one-day cricket international in which England faces the touring Pakistani team at Edgbaston, Birmingham. Many, perhaps most, of the 13,000 spectators at the game will be British Pakistanis cheering on the tourists. The match starts at 2pm and finishes at 10pm. Polls close at 9pm.

For the People's Justice Party, whose candidate and support are drawn from among the Kashmiris who make up most of Birmingham's Pakistani population, the coincidence could spell disaster. The PJP says it therefore tried to get Labour to support it in lobbying for a postponement of the match, but Labour denies that it was approached. Still, Labour knows that the Kashmiris are fed up, and that the PJP is on a roll. It is therefore, presumably, hoping for a fine day and a long match.

Birmingham's Kashmiris are one of a number of groups who feel that the mainstream parties have ignored them. Some of those groups are not natural Labour supporters. The egg that hit John Prescott, the deputy prime minister, on May 16th was fired by a furious ferret-keeping farm worker. But Labour is also under pressure on its home ground. Tony Blair was confronted in front of the television cameras in a safe Labour seat in Birmingham by a woman distraught by the National Health Service's treatment of her husband—a place, and an issue, which Labour considers its own.

Labour always knew that, by shifting to the right, it would alienate some of its core supporters, but it thought it could afford to because those old Labour loyalists would have "nowhere else to go". The hope was that anger would subside into apathy. But some of those angry people are looking less and less likely to stay at home on June 7th. In the West Midlands, at least, they are getting organised, and beginning to worry Labour candidates.

The PJP was formed only in 1998. Since then it has already won five council seats, mostly in the Sparkbrook and Small Heath constituency held by Labour's Roger Godsiff. It is contesting three seats in inner-city Birmingham, but will be concentrating most of its campaigning efforts on Mr Godsiff's territory.

The PJP was originally called the JFK, which stood, approximately, for "Justice for the Kashmiri Community". Around 120,000 of Birmingham's 1m people are Kashmiri-origin Muslims. The PJP claims that about 40% of the voters in Sparkbrook and Small Heath are Kashmiri. Its candidate is a young, charismatic youth worker called Shafaq Hussain. He argues that the party's support is almost entirely made up of formerly "loyal Labour card-holders and activists". Labour took the Kashmiri vote for granted in the past, and the Kashmiris know it.

But the party, as its name-change suggests, is trying to broaden its appeal. It argues that Birmingham is a "divided city". While the city's Labour politicians preside over the building of the huge, shiny new Bull Ring shopping precinct in the city centre, Sparkbrook still has some of the country's most run-down estates, as well as some of its highest rates of unemployment. Labour's record of economic stability and fiscal prudence does

not impress in Sparkbrook.

Nor has the nasty row about the selection of Khalid Mahmood, the new candidate for the safe seat of Perry Barr, done Labour's standing any good in the city. Even by the usual unfraternal standards of the Birmingham Labour party, the atmosphere is poisonous. Mr Godsiff's only printable epithet for Jeff Rooker, the retiring MP for Perry Bar, who has refused to support Mr Mahmood, is "that little runt".

In 1997, the emblematic independent was Martin Bell, a former journalist in a trademark white suit. This time round, in the constituency of Wyre Forest, just to the south-west of Birmingham, it is a man in a white coat. A local doctor, Richard Taylor, is standing as an independent candidate in protest over the closure of the local hospital's accident and emergency unit.

Over the past two years, Mr Taylor has channelled local fury at the closure of this unit into a campaign group called Health Concern. The group has won 17 seats on the Wyre Forest District Council, which it now runs in coalition with the Liberal Democrats. For the general election, the Liberal Democrat candidate has stood down to give Mr Taylor a free run at Labour, which won the seat in 1997 with a majority of 6,946. Mr Taylor has a good chance of victory. Like the PJP, he has something important behind him—momentum, which American political commentators call "the big mo", and to which they attribute an almost mystical power.

Mr Taylor has the mystical power of the big mo

David Nellist, the Socialist Alliance candidate in Coventry North East, is not surfing to Westminster on a wave of support, but he could still do Labour some damage. He has a big personal following in the area, which he represented for Labour in Parliament until he was expelled from the party in 1992 for his association with the left-wing Militant Tendency. The Socialist Alliance has also been picking up council seats in Coventry, and Mr Nellist is adept at mobilising the support of those working-class Labour voters who feel Mr Blair no longer represents them.

These parties have nothing much in common beyond a desire to punish New Labour. The PJP, in particular, cannot even unite the local Muslim community, let alone other disaffected voters. But they may take a seat or two; and they feel like the beginning of something that the government may have to pay attention to.

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Campaign diary

On the trail

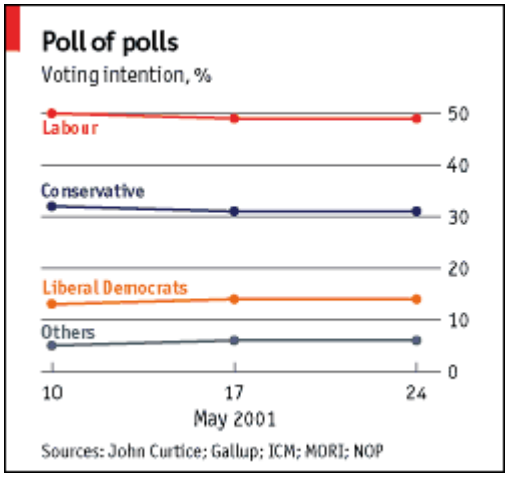
May 24th 2001
From The Economist print edition

Pledge of the week

Jordan (not her real name), a pneumatic glamour model more often seen in the company of football players than politicians, was one of the hopefuls to declare their candidacy before the deadline. She is standing in the Stretford and Urmston constituency, on a promise of free plastic surgery for all. “I know it will take a big swing to win the seat,” she says, “but there’s no bigger swinger than me.”

Plebeian of the week

The efforts of Shaun Woodward to secure the seat of St Helens South for Labour have been dogged by allegations about his wealth, and consequent incompatibility with the working-class constituency. Anxious to fit in, Mr Woodward has denied rumours that he has a butler: the idea, he says, was “an invention of Tories who still live in the world of P.G. Wodehouse”. There is no butler: “We just have three people who look after the house.” Just like everybody else in St Helens, then. Meanwhile, a group of “rapid-reaction butlers”, despatched from Conservative central office, were said to be seeking out Mr Woodward after hiring butler outfits.



Whinge of the week

Margaret McDonagh, general secretary of the Labour Party, wrote to broadcasters expressing concern that they might be colluding with anti-Labour protesters, and overstepping the line between making and reporting news. After all, what other possible explanation could there be for last week's angry confrontations between ministers and the public?

Manifesto of the week

The Monster Raving Loony Party launched its election-winning platform this week. The two leaders, Alan “Howling Laud” Hope and a ginger tabby, Cat-Mandu, promised to reduce class sizes by making children stand closer together. And they offer a compromise on hunting: the sport would not be banned, but would be made fairer by allowing only one dog per fox.

Socialist of the week

“Obviously it would be good if people didn't have to pay any tax at all.”

Tony Blair, the prime minister

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Asylum

Lunatic

May 24th 2001
From The Economist print edition

The argument on asylum is nonsensical and dishonest

A FORMER Conservative immigration minister recalls cartloads of files being wheeled past him, so that officials could “truthfully” reply to parliamentary questions that the files had personally been reviewed by the minister. The debate over asylum during the election campaign is similarly surreal.

William Hague’s promise that a Conservative government would provide “a safe haven, not a soft touch” is based on locking up all asylum seekers in secure reception centres. Various objections have been raised: that the idea of jailing thousands of innocent people, many of them torture victims, sits uncomfortably with Britain’s self-image as a haven for the persecuted; that the courts, which have been vigilant in safeguarding the rights of refugees, would likely overrule such a policy; that the plan is plainly impractical.

At present, there are around 70,000 asylum applications a year. Including dependents, that is more than 100,000 people. On average, each asylum application takes 14 months to process. The shadow home secretary, Ann Widdecombe, has estimated that only 4,000 secure places would be needed to detain all applicants, but it is not clear how that figure was arrived at. Even if universal detention cut the inflow by half and even if the time for processing their applications was also cut by half—both questionable assumptions—more than 25,000 prison places would be required. That would be a 40% increase in Britain’s prison population. The Conservatives have not explained how much it would cost to provide these places or where they would be built.

Nick Hardwick, chief executive of the Refugee Council, says the detention policy is “fundamentally dishonest” because the Tories know they are not going to have to implement it. “It’s more about creating mood music around the issue than anything else.” So far the Tories have succeeded in setting the mood. Asylum is one of the few policy areas in which they are clearly ahead.

Jack Straw is trying to close the gap, both, it seems, in the polls and in the policy. He was recently reported as saying that he wanted to cap the number of refugees Britain accepts each year. That has now been denied but ministers are hinting that they want to rewrite the Geneva Convention on Refugees to limit Britain’s obligations to accept asylum seekers. As there are more than 160 signatories, the chance of a successful renegotiation is remote. But plausibility is not the main criterion in the competition to devise ever-tougher asylum policies. Refugee lobby groups say they can’t wait until the election is over.

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Nationalism

Dragon's teeth

May 24th 2001 | EDINBURGH AND CARDIFF
From The Economist print edition

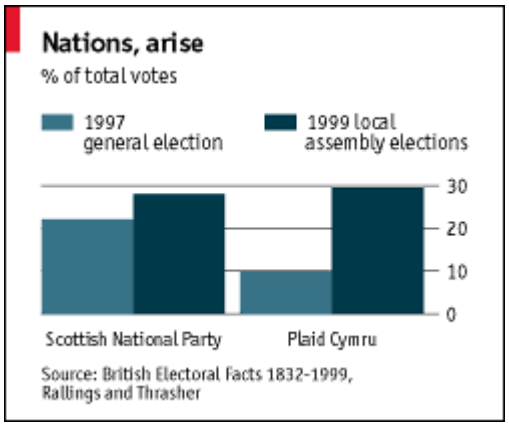
In Wales more than in Scotland, the nationalists could make trouble for Labour

PLAID CYMRU, the Welsh nationalist party, is used to the Scottish National Party (SNP) getting all the British media's attention at election time. The SNP is a lot more explicit about wanting Scottish independence than Plaid is about its plans for Wales, and it got a much bigger share of its countrymen's vote in the 1997 election—22% to Plaid's 10%. But at this election, it looks as though it will be the Welsh who give Tony Blair the bigger headache.

At first sight, both of the Celtic fringe parties appear to be struggling to make headway. They have new and relatively unknown leaders—Ieuan Wyn Jones for Plaid and John Swinney for the SNP—without much television presence. Devolution has also presented the nationalists with a problem. Scots and Welsh voters tend to see the devolved assemblies in Edinburgh and Cardiff, rather than Westminster, as the nationalists' natural home. Neither party will get anything like the vote (28% for the SNP and 29% for Plaid) that it got in the 1999 assembly elections.

So, among the claims that Mr Blair will be anxious to make on June 8th will be that the nationalists have suffered a serious setback after the upward surge in their vote in recent years (see chart). But the reality looks likely to be rather different, more so in Wales than in Scotland.

The SNP may get more votes than in 1997, but it will struggle to win seats. Its best hope is Labour-held Inverness East, Nairn & Lochaber. But, because the hostility to the Tories that led to so much tactical voting in 1997 has abated, any gain there may well be offset by losses to the Conservatives in Galloway & Upper Nithsdale, and Perth.



The same shift in attitudes in Wales could allow the Tories to win back Ynys Mon (Anglesey) from Plaid. But the nationalists have a different target in mind in this election—winning enough votes from Labour to set themselves up for a tilt at power in the 2003 assembly elections in Wales and Scotland. As yet, there is little sign that the SNP is liable to do real damage to the Scottish Labour party, but Plaid has already broken through in Labour's Welsh heartlands and seems set to consolidate its bridgehead on June 7th.

The party is reasonably confident that it will pick up two rural Labour-held seats it won in 1999—Carmarthen East & Dinefwr, and Conwy. It is also excited about its chances of getting close to repeating its stunning feat in 1999 when it won three assembly seats—Islwyn, Rhondda and Llanelli—in the Labour stronghold of the south Wales valleys.

There are reasons why Labour is more vulnerable in Wales than Scotland. Apart from Paul Murphy, the Welsh secretary, the Welsh Labour party does not have the big players in government, such as Gordon Brown, the chancellor of the exchequer, and therefore the stake in Mr Blair's New Labour project, that the Scots have. This feeling of remoteness from the government was made worse by Mr Blair's ham-fisted imposition in 1999 of Alun Michael over the popular Rhodri Morgan as Welsh Labour leader.

Although Mr Michael was ousted last year and Mr Morgan is now first minister in the Welsh Assembly, the memory still smarts. Barry Jones, a lecturer in politics at the University of Wales in Cardiff, reckons that this, combined with Mr Blair's centrist policies, tells a lot of Welsh voters that the Labour Party they voted for does not exist any more.

At the same time, the Welsh Assembly allows voters to see a lot more of Plaid Cymru in action. They are discovering that it is left-leaning, sensible-looking, and not the nutty sect of Welsh-language zealots that Labour had warned them to stay away from.

John Osmond, director of the Institute of Welsh Affairs, says that in Welsh politics, the opponents of the establishment usually win the prizes. Labour is now clearly identified as the establishment, but turned out to be powerless when Corus, a British-Dutch steel firm, announced in February it was getting rid of 3,000 Welsh steel-making jobs. That still hurts in the valleys. Come polling day, Mr Blair may share the pain.

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Bagehot

How not to save the pound

May 24th 2001
From The Economist print edition

The Conservatives are making it more likely that Britain will scrap the pound and adopt the euro

AS YOU can imagine, many absorbing press releases about this and that have landed on Bagehot's desk since the start of the present election campaign. But only one has been significant in the way that Sherlock Holmes found the failure of the dog to bark in the night significant. This was the one whose sender promised to say nothing until the campaign was over.

The sender was the "No" campaign, the name under which two anti-euro pressure groups—Business for Sterling and New Europe—campaign jointly against British membership of the European single currency. In their press release, the two groups briskly remind the press that they are not involved in the general election, that neither endorses a political party, and that they exist only in order to campaign against Britain's membership of the European single currency. For the duration of the election, they have, in effect, taken a vow of silence.

This is curious. One thing that has made this election feel flat is that the parties look alike on so many issues. The euro is a glorious exception. Here voters face a stark choice on a question that will have fateful consequences however they answer. Tony Blair says that if he is re-elected, and provided various economic tests are met, a Labour government will propose in a referendum that Britain should adopt the single currency. William Hague promises that a Conservative government would keep the pound. The choice could hardly be plainer. Or could it? One non-plain thought prompted by the vow of silence from the "No" campaign is that the Conservatives are in fact making it more likely, not less, that Britain will one day join the euro.

To unravel this paradox you have to accept the evidence of the opinion polls that the Conservatives are heading for defeat. If they were somehow to win, Mr Hague would indeed go down in history as the dauntless saviour of the pound (and as a political Houdini). But if, as expected, he loses, the interesting question is what impact this will have on a referendum later on.

Certainly, a Conservative defeat in the election is not enough, on its own, to sink the pound. The very polls which show that Mr Blair will be re-elected next month also show how many more minds the prime minister must change before he can be certain of winning a referendum. On MORI's latest figures, 70% oppose Britain's joining the euro. When, after the election, groups such as Business for Sterling and New Europe come out of purdah, the No campaign will still have public opinion on its side, as well as some decent arguments. All the same, it will be in a weaker position than before.

Mr Hague intends in the final fortnight to fight the election as if it were the referendum on the euro. Such a strategy makes eminent sense, for him. Ruling out British membership is not only his most popular policy, but also the one that enticed Lady Thatcher to rise this week from the political dead and bestow a rare personal endorsement. Though unlikely to change many votes on polling day—only a Martian could be surprised by her loathing of the euro—this could come in handy for Mr Hague when his leadership is questioned the morning afterwards.

The pound has plainly been good for Mr Hague. But has Mr Hague been good for the pound?

It is hard to see how. At a stretch, it is just about imaginable that a good Tory showing in the election would scare Mr Blair off his promised referendum. It is not altogether impossible that the Conservatives will argue so well against the euro in the remainder of the campaign that, even if they lose, public opinion on this issue can never be reversed. But these are the outer fringes of what is possible. It is far likelier that by choosing to fight the election on the euro, and then losing heavily, Mr Hague will have damaged the No campaign by associating it indelibly with his own doomed cause.

That fellow has nothing to do with me

All of this makes the silence of the No campaign a lot easier to understand. New Europe and Business for Sterling have long stressed that their support comes from all corners of politics: leading lights include Lords Owen and Healey, both former Labour ministers. The last thing they want is for the unpopularity of Mr Hague to rub away the popular objection to the euro.

There is, however, yet another danger. Has Mr Hague contaminated the sound arguments for a No in the referendum by spraying so many unsound ones in the general direction of all matters European during the election?

When it comes to the referendum, the merit of Lords Owen and Healey is not only that they are not Conservatives. It is that they are Good Europeans who nonetheless oppose British membership of the euro. Like Mr Hague, neither deems it in Britain's interest to submit to every demand the EU makes for "ever-closer union". But unlike Mr Hague, they do not express their objections in the juvenile language of nationhood in peril.

Naturally, Mr Hague disavows the opinion of Sir Peter Tapsell, a veteran Conservative MP who accuses the German chancellor, Gerhard Schröder, of trying to achieve by peaceful means the domination that Hitler failed to impose on Britain by violent ones. But Mr Hague does believe that the EU threatens to make Britain "a foreign land". Though he says he cannot conceive of Britain leaving the EU, many senior people in his party desire just that.

No doubt historians will argue in defence of Mr Hague that his exaggerations and ambiguities on Europe kept a divided party together and turned what used to be a political liability into an advantage, albeit not a big enough advantage to win this election. Against this, he has fallen into the trap of reinforcing the myth, cultivated by Mr Blair, that to oppose British membership of the euro is to oppose British membership of the EU itself. There could be no better way for the Conservative leader to destroy the pound he claims to love.

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The queue for the cabinet

New Labour, (some) new faces

May 24th 2001
From The Economist print edition

PA

Merit alone is not always enough to secure a place in the cabinet

ALL MPs fight for re-election as if their jobs depended on it, which, as it happens, they do. Some Labour MPs will try that little bit harder in coming weeks. These are the MPs who aim not only to impress voters but to catch the eye of Tony Blair, in the hope that he will put them in the cabinet. But although no prime minister wants duffers around his table, such jobs are not always awarded on ability alone. Among other factors Mr Blair is liable to take into account are:

•**Sex**. Although Labour boasted in 1997 of its record crop of 101 women MPs, only five made it into the cabinet. One, Harriet Harman, was later sacked from her job as secretary of state for social security, and another, Margaret Beckett, was demoted from secretary of state for trade and industry to leader of the House of Commons. Labour's leader in the House of Lords, Lady Jay, is giving up her job, and Mo Mowlam decided when she was recalled from Northern Ireland that she would retire after this election. Clare Short may hang on as secretary for overseas development, but did not help her cause by saying on a radio show last week that the prime minister's controversial decision to announce the election at a stage-managed event in a girls' school had been "odd".

If Mr Blair wants new female faces in his cabinet, an obvious choice is **Patricia Hewitt**, the energetic 52-year-old minister responsible for small business and e-commerce at the Department of Trade and Industry. Though an MP only since 1997, she experienced Labour in-fighting at its roughest as Neil Kinnock's press secretary and adviser in the early 1980s. Working for the party leader made her take against its tribal ways, which should appeal to the moderniser in Mr Blair. She is more of an all-rounder than **Estelle Morris**, a former teacher who looks like a girl guide but is as tough as an old blackboard and has done a good job of taking on the teachers' unions as a minister in the Department of Education and Employment.

Lady Symons, minister of state for defence procurement, is a candidate to replace Lady Jay. She would feel at home in Downing Street, having recently married Phil Bassett, her long-term partner and senior member of the Number 10 spin-doctorate (who has in turn been tipped as a successor to Alastair Campbell as the prime minister's official spokesman). Capable of steely charm and the occasional tantrum, Lady Symons was general secretary of the First Division Association, the top civil servants' trade union, before Mr Blair gave her a peerage.

•**Colour**. If Mr Blair wants a black face in his cabinet, he will consider **Paul Boateng**, a former barrister who has received reasonable reviews as deputy home secretary. But Mr Boateng has been savaged by sketchwriters for an arrogant manner and hectoring tone. Another possibility would be to give the job of leader of the Lords to **Lady Scotland**, a sparky barrister who became a QC at 35 and is now a junior minister in the Foreign Office. But Lady Symons is above Lady Scotland in the hierarchy. And both women may lose out if Mr Blair can think of no other way to bring into his cabinet **Lord Macdonald**, the Glaswegian trade unionist turned media tycoon turned transport minister.

•**Guilt**. Do prime ministers ever feel this? That would help **Nick Raynsford**, the minister for housing and planning, a master of detail who designed most of Labour's devolution plan for London and steered the legislation through Parliament. In a moment of madness, Mr Blair let the schoolmasterly Mr Raynsford say that he would stand for London mayor, only to shunt him aside by telling **Frank Dobson**, then health secretary, to stand instead. There are reports in the *Sun*, Labour's official gazette, that Mr Blair might make amends to Mr Dobson by bringing him back to the cabinet as chief whip. This would be a blow to **Adam Ingram**, the minister of state for Northern Ireland, who was passed over for the top job there and hoped for the whip's job. **Michael Meacher**, a formerly Bennite member of the shadow cabinet fobbed off with a junior job in 1997, may have earned promotion by his deft handling of green politics.

•**Personality**. If the young men promoted during the first term—Alan Milburn (health), Stephen Byers (trade and industry), Alistair Darling (social security) and Geoff Hoon (defence)—have impressed as technocrats, they have disappointed as political personalities. The rough-hewn **Charles Clarke**, a burly, bearded Home Office minister, responsible at present for driving reform through the police service, who learned the black arts of Labour politics as Mr Kinnock's chief aide in the 1980s, might make more of a splash. His prospects have been helped by the departure of Peter Mandelson, an old friend with whom he fell out. Those of **Peter Hain**, the famous battler against apartheid who portrayed himself latterly as a bridge between New Labour and its doubting heartlands, seem to have waned since his demotion from the Foreign Office to energy minister. Which leads on to:

•**Political balance**. One factor that may no longer matter. In his first term, a cautious Mr Blair put old war-horses such as John Prescott in the cabinet to placate the old left. A second massive endorsement by the voters of Middle England should make such calculations redundant. To that extent at least, Mr Blair's next cabinet could be a model of the meritocracy he says he would like Britain to become.

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Taxation

Where's the money coming from, Gordon?

May 24th 2001
From The Economist print edition

The Tories drew blood on tax this week

ASSUMING that the economy grows at the rate that the Treasury thinks it will, and assuming that the government keeps on increasing public spending at the rate it plans until 2003, Labour will need to raise taxes during the next Parliament. But how, without infuriating the middle-class voters who will vote Labour back into power on June 7th?

Gordon Brown, the chancellor of the exchequer, dismissed as a "typical Tory election smear" the suggestion that he would in effect introduce a 50% top income-tax rate by scrapping the ceiling on National Insurance contributions paid by employees. His intervention followed an uncomfortable two days in which the Tories exploited his initial reluctance to rule out changes to the NI ceiling.

Although Mr Brown stopped short of pledging that he would not abolish the NI ceiling, his words would surely haunt him if he were to do that in office. In any case, he probably has something different in mind: to align the NI ceiling with the threshold for the higher income-tax rate.

At present, employees pay NI contributions at 10% on annual earnings between £4,524 and £29,900. However, this ceiling is about £4,000 lower than the income at which people start paying the 40% top rate of income tax. That means that the overall shape of the NI and income-tax schedule is peculiar. Most earnings up to £29,900 are taxed at 32%, the joint rate of NI contributions (10%) and the basic rate of income tax (22%). However, the next £4,000 tranche of earnings is taxed at 22%, the basic rate. On earnings above £33,935, the tax rate jumps to 40%, the top rate of income tax.

This kink in the NI and income-tax schedule makes little sense. But aligning the NI ceiling and the higher income-tax rate would not raise much money, any more than it would be a big blow to the taxpayers affected. It would increase government revenues by only about £1 billion.

Abolishing the NI ceiling would raise about £4 billion, but if the government needs that sort of money, it is more likely to increase NI contributions paid by employers. These amounted to £34 billion in 2000-01, substantially more than the £25 billion paid by employees and the £1 billion paid by the self-employed. Furthermore, they are a less noticeable tax, even though much of any increase would eventually be passed on to employees through lower pay rises. "It's not easy to whip up a head of steam about employer NI contributions," says Edward Troup, a tax adviser to Kenneth Clarke, a former Tory chancellor. "They are a remarkably easy tax to raise without any visible effect."

Mr Troup also thinks that tobacco duties and the insurance-premium tax that Mr Clarke himself introduced are "obvious candidates" to raise some extra money. Mr Brown would be hard-pressed to find another stealth tax to match his removal of dividend tax credits for pension funds in his first budget in 1997. That pocketed a handy £5.5 billion a year and no one appeared to notice. But the Treasury's cupboard is not bare yet.

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Policy watchdog

Anti-spin

May 24th 2001
From The Economist print edition

The Institute for Fiscal Studies is the country's unofficial economic referee

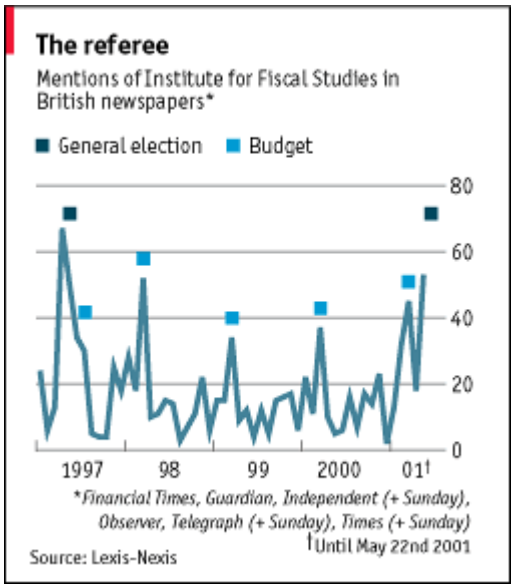
IF WALTER BAGEHOT were mapping today's unwritten British constitution, he might include a reference to the Institute for Fiscal Studies. The London-based IFS has come to play a distinctive role in Britain's elections. For journalists trying to disentangle the claims and counter-claims of politicians against hourly and daily deadlines, it has become an indispensable source of anti-spin.

Inevitably, this means that the IFS ends up in the political scrum. The day after Tony Blair called the election, it brought out special election briefings comparing the fiscal record of the last parliament with previous ones. The Conservatives seized on its finding that if Labour were to continue increasing spending after 2003 at the same rate as over the next three years, taxes would have to rise by £5 billion a year. This was just arithmetic, insisted Andrew Dilnot, director of the IFS. To the Tories, however, it was proof positive of a £10 billion "black hole" in the government's spending plans.

A week later, the IFS cast a beady eye over the Conservatives' claim that they could cut spending by £8 billion by 2003 while matching Labour's spending plans for the main public services. Now it was Labour's turn to draw upon an assessment by the IFS. In a mock presentation this week of a Tory "boom and bust" budget, Alistair Darling, Labour's social security secretary, invoked the institute's sceptical analysis about the savings that could be achieved from privatising the New Deal programme for young people.

For a research organisation that exerts this degree of influence, the IFS is surprisingly small, with a budget of only around £2.5m and 25 full-time staff. Established in 1969, it has gained particular prominence in the past ten years as tax and spending have become the central battleground of elections (see chart). Its influence stems as much as anything from a studied neutrality in the bitterly contested battleground of tax and spending. Mr Dilnot says: "One of the things we're doing is helping people to understand and make sense of a range of often apparently contradictory figures." That's a polite way of saying that politicians are notorious for their selective use of statistics.

Arguably, this dogged pursuit of neutrality exacts a cost. The IFS eschews some of the important questions that need to be asked, such as how big the state should be, saying that this is a political question. Maybe so; but it is also an issue on which economic judgments can be passed. Mr Dilnot accepts that the IFS does pay a price for leaving this debate to others, but says that it is a price worth paying to ensure the institute's reputation for objectivity.



In effect, the IFS has filled the vacuum caused by the loss of credibility of politicians bearing numbers. MPS could do something about this. The next parliament could set up the equivalent of America's Congressional Budget Office. The CBO is expressly charged with providing objective, non-partisan analysis about the public finances to the powerful committees of the Congress. However, the last thing a newly elected government would do is to arm MPS at Westminster with a similar source of unvarnished information. The IFS looks set to retain its curious niche in Britain's curious constitution.

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The fight in Hartlepool

Mandelson Agonistes

May 24th 2001 | HARTLEPOOL
From The Economist print edition

One of the more colourful election battles is taking place in Hartlepool

IT IS hard not to feel a bit sorry for Peter Mandelson. When last he was obliged to resign from the government, he expressed a wish to eschew the whirligig of Westminster for the haven of his Hartlepool constituency. He is now involved in an electoral tussle so surreal that Mike "The Mouth" Elliott, a comedian who considered participating, decided not to, because the contest had become a circus.

Bankruptcy prevented Neil Hamilton, an icon of Tory sleaze, from standing in Hartlepool. But the candidates include a former Labour press officer, whom Mr Mandelson once sacked, and who is vigorously impugning his integrity. Gus Robinson, a local property developer, boxing promoter, Conservative, and probably Mr Mandelson's main rival, leavens his sound-bites with allusions to the Bible and colourful anecdotes—like the one about local hoodlums threatening to decapitate him with a shovel. "I'll take them all on," he says, referring to the Cabinet. Amid mutual allegations of carpet-bagging, Nigel Boddy, the Liberal Democrat, cites a grandfather who defended Hartlepool from the German bombardment of 1914.

Then there is Arthur Scargill, general secretary of the Socialist Labour party, and (still) president of the National Union of Mineworkers—a champion of socialism or its greatest embarrassment, depending on your point of view. Mr Scargill's party, which is fielding 114 candidates, offers full employment and a four-day week, as well as abolition of the monarchy, withdrawal from the EU, and an orgy of re-nationalisation. "You can vote for one of three Conservative candidates," Mr Scargill says, "or you can vote for me."

This duel between the avenging angel of Britain's hard Left and the prodigal New Labour prince has an obvious symbolic appeal. The contrast of old industrial angst and slick modernisation also encapsulates Hartlepool's own schizophrenia.

The town boasts a swanky new marina and quayside museum, encircled by shiny, gigantic retail slabs, and a multiplex cinema. The regeneration began under the Conservatives, but in the past four years Hartlepool's schools have improved, and regeneration money from various government pots has been secured.

Away from this nirvana, though, Hartlepool, like other towns in the region, still suffers from the decline of heavy industry, whose remnants form an incongruous backdrop to the marina. It remains one of the country's most deprived towns: unemployment, though falling, is more than double the national average, with stubborn pockets of inter-generational joblessness. Round the corner from Mr Mandelson's home are rows of boarded-up terraced houses which sell for as little as £14,000. Pawnbrokers abound.

They hang monkeys, don't they?

Mr Mandelson insists that there are no irreconcilable differences between him and the less sophisticated town. His Europhilia probably has limited appeal in a place whose residents, according to local legend, once hanged a shipwrecked monkey as a Napoleonic spy. But Mr Mandelson says he has never suffered xenophobic hostility. Some locals complain that the region has not obviously benefited through the many Cabinet ministers whose (safe) seats cluster in the north-east. Mr Mandelson says he uses his "voice and sharp elbows" to Hartlepool's advantage. He now embraces the ideas of a "north-south divide" and devolved regional government—both of which alarm some Labour politicians. There is, he claims, a "real sense of grievance" about his own travails among the constituents.

A majority on the scale of Mr Mandelson's—17,508—ought to be safe, other than in exceptional circumstances—such as, say, being ejected from the Cabinet twice in one parliament. The Tories are hopeful that Mr Mandelson's scalp might prove to be the equivalent of Michael Portillo's talismanic defeat in 1997. Even so, and despite Mr Robinson's energy and pugilistic credentials, the contest is probably as much of a mismatch as that between Hartlepool and Mr Mandelson, whose campaigning skills, complete with the occasional modulation of accent, are as formidable locally as they have proved nationally.

Hartlepool is unlikely to hang New Labour's organ-grinder. And Mr Mandelson is determined to see off not just the other candidates, but also the conspiratorial forces he says have tried to "drive [him] out of politics". (The Hartlepool circus suggests that this paranoia may be partly justified.) He says he now wants to "lead a more normal political life"—though he agrees that he is addicted to the sort of struggle from which he claims to be escaping: "I cannot see myself settling for an easy life." Mr Mandelson, like Mr Scargill, is not prepared to await the vindication of history. But, like Mr Scargill, he may not have much choice.

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Israel and the Palestinians

Yes to a ceasefire, no to a halt on settlements

May 24th 2001 | JERUSALEM
From The Economist print edition

Israel's responses to the latest recommendations for ending Israeli-Palestinian violence show the disunity of the unity government

Get article background

Reuters

Creating facts on the West Bank's hills

SO LONG as it was only the Palestinians who contended that an end to Israeli settlement-building would bring an end to the *intifada*, the Israelis could dismiss the notion. But now an ultra-respectable international group, led by George Mitchell, a former American senator and peace broker for Northern Ireland, has made the same connection between settlements and violence. The commission's report, published on May 21st though leaked earlier, urges a complete ceasefire to be followed by a complete freeze on further settlement-building, including construction in existing settlements.

The recommendation has predictably exacerbated the disunity between hardliners and moderates in Ariel Sharon's government of national unity. Avigdor Lieberman, the minister of infrastructure and an extreme hardliner, gave warning this week that if Mr Sharon accepted the Mitchell report the government would fall apart. Labour members threatened a crisis if he did not accept it. So Mr Sharon and Shimon Peres, his Labour deputy, are trying to devise a policy that will reconcile acceptance with non-acceptance, and get their parties—and the rest of the world—off their respective backs.

On May 22nd Mr Sharon called publicly for an immediate ceasefire. Privately, he ordered the army to stop any further offensive actions. The soldiers were to shoot only if they were in direct danger, his officials said, and Mr Sharon would allow "several days" to see how the Palestinians reacted to his gesture. It did not take that long: the next day, Palestinian gunmen killed an Israeli contractor driving in the West Bank, and a fierce battle in Gaza left several Palestinians wounded.

In his public statement, Mr Sharon also said that, if there were a complete ceasefire that held up through a "significant cooling-off period", he would then be prepared to discuss the Mitchell report's confidence-building measures, among them the settlement freeze. He was sure, he said, that a way could be found to accommodate the "ongoing needs" of the settlements while allaying Palestinian fears that more construction would close off negotiating options. No new land need be requisitioned for further home-building: "There is quite enough available." But if bypass roads needed to be built, for security reasons, then land would "certainly" be taken.

The prime minister pointedly praised Colin Powell, America's secretary of state, for emphasising, a day earlier, that the commission's call for a ceasefire was not dependent on the recommended settlement freeze (see article). America's ambassador to Israel, Martin Indyk, its consul-general in Jerusalem, Ronald Schlicher, and the new special assistant for the Middle East, William Burns, are to start shuttling between Israel and the Palestinians.

For his part, Mr Peres claims that the Mitchell report will be adopted by both sides, and will lead to a speedy resumption of peace negotiations. Building work, he maintains, can quietly continue within existing settlements, so long as it does not mean new land expropriations.

But the Palestinians have dismissed Mr Sharon's ceasefire call as a public-relations stunt, accusing him of tendentious selectivity in his ostensible acceptance of the Mitchell plan. They have called for the adoption of the Mitchell proposals as an integral whole, and for an international summit to devise "a practical mechanism" for implementing them. Yasser Arafat, on the telephone to George Bush, appealed for the president's personal intervention.

A similarly sceptical view of the Israeli government's position came from Israel's opposition leader, Yossi Sarid. Mr Sharon, he said, had no genuine intention of accepting the Mitchell report; he was merely pretending to accept it while emptying it of all significance. Mr Peres, too, was pretending: since much of the land on the West Bank had been designated "state land", no further expropriations from individuals were required to continue building. "The world won't buy this bullshit," said Mr Sarid, "and nor do I. The Mitchell report is the last hope to avert full-scale war."

Mr Sarid's harsh tone chimed with the widespread and angry domestic criticism of Mr Sharon for ordering F-16 fighter-bombers to bomb targets in several Palestinian towns on May 18th, after a suicide-bomber had killed five Israelis at a shopping mall in the coastal town of Netanya. This was the first time that warplanes had been used in the eight months of the *intifada*, and it left many Israelis aghast.

Twelve Palestinian policemen were killed in the air raids, and hundreds of civilians injured. One target was a prison in Nablus where a prominent Hamas terrorist was reportedly being held; he was apparently not hurt, if he was there at all. Israeli newspapers reproached Mr Sharon for reacting with his gut rather than his head. "What do we do next week," asked Dan Meridor, chairman of the Knesset foreign-affairs committee, "if there is a worse terror attack, with more victims?"

The discomfort at the way Mr Sharon and the army are fighting the *intifada* was intensified on May 20th when an Israeli tank fired two shells at the Ramallah home of Colonel Jibril Rajoub, head of the Palestinian security force in the West Bank and a central figure in what remains of the Israeli-Palestinian dialogue. He was taking a shower, but escaped unscathed. Just hours earlier he had welcomed Israeli journalists at his office for a briefing, in the fluent Hebrew he learnt in jail. The army said there had been repeated shooting from a position close to the house. There was no intention of hitting Mr Rajoub, whose force has consistently stayed out of the fighting. Awkwardly, though, the officer in command of the tank unit told a radio interviewer that his men did in fact know whose home they were firing at.

The decision to use warplanes was taken by the "kitchen cabinet", which comprises Mr Sharon, Mr Peres and the minister of defence, Binyamin Ben-Eliezer. All three doggedly defended the action. Other ministers, not in the loop, muttered their reservations, both over this and over the sophistry with which the Mitchell recommendations have been met. "We're in this government to protect our principles," said Labour's Matan Vilnai, the minister of culture and another ex-general. "If the government doesn't accept the Mitchell report in full, we shouldn't be there."

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America and the Middle East

A toe in the water

May 24th 2001 | WASHINGTON, DC
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Colin Powell's cautious words on the Mitchell report

BY APPOINTING a special envoy to the Middle East and by endorsing the Mitchell report on the Israeli-Palestinian conflict, America's secretary of state, Colin Powell, has made two small shifts in policy. It is still unclear how far he is willing to go on the bigger question of whether America is prepared to intervene to stop the fighting.

Reuters

Powell goes in gingerly

But at least the Bush administration has abandoned its initial hope that it could ignore Israel and Palestine in order to concentrate on Iraq. Little has been heard of that idea since Mr Powell's trip to the Middle East in March. Linkage between one Middle Eastern issue and another is, he discovered, rather strong in the minds of some 200m Arabs.

Over the past few weeks, the administration has been torn between increasing international pressure to step in, and its own fear of failure. The fear is born partly of Bill Clinton's experience, but is also the result of its own—not unreasonable—assessment that the chances of a breakthrough are small.

The Mitchell report offered a way out of the dilemma. Since it was a United Nations document, Mr Powell could endorse it without adopting it wholesale. Above all, he stopped short of endorsing its central and most controversial element, the proposal to freeze all Jewish settlement activity. Mr Powell merely said that settlements were a problem. He offered no American plan to end the fighting. Nor did he appoint a special envoy, in the sense of someone (like Dennis Ross, Mr Clinton's envoy) who had exceptional political status and reported directly to the White House.

Instead, he asked William Burns, his assistant-secretary-designate for Near Eastern affairs, to work out how to help implement the Mitchell recommendations, which, among other things, call for an unconditional ceasefire, and require the Palestinian Authority to arrest terrorists operating in its areas. But Mr Powell has not committed his own authority, still less that of his president.

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Egyptian security

Shutting up Saadedin

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Egypt jails an outspoken civil-rights campaigner

IN THE mid-1990s Egypt's government faced a violent insurgency by Islamist militants. Over 1,000 Egyptians died, and many more were arrested and tortured. The unrest eventually fizzled out. What has lingered is the heavy hand of the state's security apparatus.

A reminder came this week with the sentencing of a prominent civil-rights activist to seven years' imprisonment. Saadedin Ibrahim, a 62-year-old sociology professor, had been arrested last year, along with 27 employees of the research institute he ran, and charged with a clutch of crimes ranging from fraud to "defaming Egypt's reputation". He was thought to have raised particular ire by championing the Coptic Christian minority, by calling for openness in Egypt's famously murky elections—and by attracting generous financing from western donors, including governments.

The sentences, which included shorter terms in prison for six of his associates, have raised fears that Egypt's security services have widened their brief dangerously. Arrests at gunpoint, charges under emergency laws, and trials with no right of appeal have long been the fate of religious militants. In recent years the scope of summary justice has grown to include urban professionals from the Muslim Brotherhood, a shadowy but powerful group that seeks "Islamic" rule by peaceful means.

Such harsh methods are increasingly being used against less obvious threats to the state. Recent victims include teenagers accused of satanism, homosexuals, a series of unlikely "spies" for foreign agencies, and businessmen tarred with flimsy corruption charges.

Mr Ibrahim may perhaps be able to appeal. The irony of the whole business is that Egypt's image is damaged much more when university professors get thrown in jail than when they point out the government's shortcomings.

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Ghana's violent past

Skeletons under the sand

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From The Economist print edition

National reconciliation in Ghana means disinterring old horrors

A VIOLENT past is about to be dug up. Petitioned by the victims' families, Ghana's president, John Kufuor, has ordered that the remains of eight generals, who were summarily executed in June 1979 on charges of treason and corruption, should be exhumed so that funerals and reburial can take place. It is a first step by Mr Kufuor, who was elected last December, to honour his pledge to bring some form of reconciliation to his people after the 19-year rule of Jerry Rawlings.

The generals, including three former heads of state, were executed at a shooting range on the beach after peremptory trials by a "people's court" set up by the Armed Forces Revolutionary Council (AFRC). The AFRC, a group of junior officers led by Mr Rawlings, then a 32-year-old flight-lieutenant, had overthrown the military dictatorship of General Fred Akuffo, who was among the executed generals. The bodies were not returned to their families. But senior prison officials announced recently that they have documents showing where the men were buried. The reburial ceremonies are expected to be held in June.

The AFRC ruled for three months before handing over to an elected civilian administration. But there was more chaos and blood-letting packed into those three months than at any time since Ghana's independence from Britain in 1957. General Akwasi Afrifa, who in 1966 led a coup against the country's first president, Kwame Nkrumah,was hauled to the beach firing range and executed for no apparent reason. Commodore Joy Amedume, chief of the navy, was executed for "using his official position to acquire a bank loan", the equivalent of $20,000.

Some think that even older skeletons should be disinterred. Enoch Mensah, an opposition member of parliament, points to the execution in the 1960s of Moses Yeboah and Samuel Arthur, who were punished for plotting to overthrow General Afrifa's government. "Why don't they go and dig them up too?" asks Mr Mensah.

But there is a more recent horror that most Ghanaians would prefer to revisit. In 1981, after Mr Rawlings, in another military coup, had overthrown the elected government that succeeded him in 1979, three judges and a retired army officer were gruesomely murdered. The four men were abducted from their homes by night, and their mutilated and charred remains were found days later in a field outside the capital, Accra.

Four people, all associated with the Rawlings regime, were found guilty of the murders. Two were executed, and the others escaped. But the judicial inquiry into the murders left many questions unanswered, and some people suggest that those who gave the orders to kill may still be walking free. The event, which traumatised Ghana's judiciary for years, is commemorated as "martyrs' day".

The attorney-general, Nana Akufo-Addo, long a campaigner for human rights, has expressed doubts whether the brains behind the murders were ever hauled in. But he says that, as in the case of the generals, individuals would have to take the initiative by presenting a petition to the government. A potential petitioner is Kwabena Agyepong, the deputy government spokesman. Mr Agyepong's father was one of the murdered judges, and he has been campaigning for years to have the killings reinvestigated.

A bill setting up a body to handle such petitions is already in the works. It seems only a matter of time before old misdeeds get a second hearing. If "national reconciliation" is handled carefully, it could indeed heal the country's wounds. If handled badly, it could tear them open again.

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Ethiopia

Post-victory turmoil

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From The Economist print edition

Domestic discontent threatens Ethiopia's ten-year-old government

AT THE height of the war between Eritrea and Ethiopia, Issaias Afwerki, Eritrea's president, predicted that the fighting would bring down his rival and former ally, Ethiopia's prime minister, Meles Zenawi. He was wrong. Mr Meles won the war last year. But now, after victory, his government is in trouble.

Divisions at the heart of his administration are exposing the fragility of his rule. Some say it is imploding. Mr Meles has been a reformer, bringing the market to a centralised state-run economy. The economy shows a healthy growth rate and the harvest will be good this year. But prices for coffee, Ethiopia's chief export, are low, and the government spent millions of dollars on the war and lost millions in aid from disapproving donors. Now the urban poor cannot afford basic goods, and unemployment is at an all-time high.

In April thousands of university students demonstrated for academic freedom on their campuses. Unemployed youths took the protest to the streets where the demonstrations degenerated into the worst public disorder for years. The government, seeing political plots behind what appears to have been a spontaneous uprising, responded brutally. Some 130 people were killed—only 31, said the government. On May 8th Mesfin Wolde Mariam, a veteran human-rights campaigner, and Berhanu Nega, an academic, were arrested, accused of stirring up the students. The two men, and hundreds of opponents of the regime, are in prison but uncharged.

On May 12th Mr Meles had more genuine grounds for fear when his head of security, Kinfe Gebre Medhin, was shot and killed at the officers' club in Addis Ababa. His death removes a close ally who kept the army subordinate to the government.

This, in turn, has exposed divisions in the government. At the administration's core are Mr Meles and his friends from Tigray, who once formed the Marxist-Leninist League of Tigray. That grew into the Central Committee of the Tigrayan People's Liberation Front (TPLF). After a long war, and in alliance with Eritrean rebels, the TPLF overthrew the Soviet-backed regime of Mengistu Haile Mariam in 1991. Originally a small separatist movement, the TPLF was suddenly faced with ruling this vast, disparate country.

Tigray is far from Addis Ababa, whose Amharic residents resented the invasion of northerners. But the TPLF created like-minded parties among each of Ethiopia's main ethnic groups until they had constructed what looked like a multi-layered, multi-party national political system. This coalition, known as the Ethiopian People's Revolutionary Democratic Front (EPRDF), has ruled ever since. But the point on which the whole rests is the secretive, all-powerful TPLF Central Committee.

This committee is now looking wobbly. When a ceasefire and peace agreement were signed with Eritrea last December, the TPLF Central Committee split and 12 members were expelled because they felt Mr Meles had sold out to western capitalism and had been weak on Eritrea. Many felt that Mr Issaias should have been crushed completely. A similar division splits the army.

The prime minister has tried to roll with the pressure, showing toughness by creating problems for the UN peacekeeping force, and by dragging his feet on the creation of a neutral buffer zone between the two countries. But that upsets Mr Meles's western allies and the UN. He needs good relations with them to get a deal out of the IMF.

Mr Meles is caught between international pressure and the demands of some of his oldest and closest allies. He tried to win support from other parties in the EPRDF, but each wanted its pound of flesh in return. His reinvented political structures have not grown deep enough roots to give him an alternative power base. Next month the TPLF and all the other parties in the EPRDF should hold congresses to celebrate ten years in power. But the dissenters are strong in Tigray, and could give the prime minister a

hard time.

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E-strategy brief: Seven-Eleven

Over the counter e-commerce

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How to blend e-commerce with traditional retailing

JUST as the Internet penetrated different countries at different speeds and in different ways, so its impact on traditional companies, the subjects of this series of case studies, has varied from one part of the world to another. Consider Seven-Eleven, a convenience-store operator, which this year snatched the title of biggest retailer in Japan from Daiei, a troubled supermarket giant.

Seven-Eleven's e-strategy is built mainly around proprietary systems. For the most part, it has used the Internet to talk to its retail customers, not to run its business. Yet few companies in Japan have been more admired for their use of electronic communications.

Unlike Daiei, and many other retailers, Seven-Eleven has managed to overcome a stuttering economy and spiralling deflation to raise sales and profits by 4% and 15% in the year to the end of February. Its pre-tax profits last year were more than double those of Fast Retailing, a clothing outlet that holds the second spot.

One reason for Seven-Eleven's sparkling performance is its cautious management. Other Japanese convenience stores, such as Lawson and FamilyMart, the second- and third-biggest, expanded recklessly over the past decade. They have recently announced the closure of hundreds of stores. In contrast, Toshifumi Suzuki, Seven-Eleven's chairman, says that he would stop opening new stores if sales at existing ones declined sharply. His caution is reflected in Seven-Eleven's finances, which are largely debt-free.

Yet solid management is not the only contributor to Seven-Eleven's success. The chain's other distinction lies in its deft use of electronics. It pioneered many techniques for using the Internet that are still ahead of the curve.

Seven-Eleven Japan was set up in 1973. By the mid-1980s it had already replaced old-fashioned cash registers with point-of-sale (POS) systems that monitor customer purchases. By 1992, it had overhauled its information-technology systems four times.

But the biggest overhaul of all took place in 1995. With hindsight, the timing looks bad: that was the year when the Internet wave was beginning to swell in the United States but had barely begun to touch Japan's shores. The new system that Seven-Eleven installed was therefore based on proprietary technology—albeit state-of-the-art—rather than on the still barely tested open structure of the Internet.

Convenience online

Back in those days—and indeed, even now—it would have been hard to build on the back of the Internet alone a system that satisfied all Seven-Eleven's complex demands. It wanted an easy-to-use multimedia system with pictures and sound, since most workers are part-timers with scant computer skills. It also wanted a system that could quickly repair itself if something went wrong.

Then the chain needed a network to speed up the transmission of orders, ideas and feedback. It wanted all the companies in its supply chain to use one common system, and it wanted a system that could be

easily updated to take advantage of technological advances. Then it wanted the system to run for at least 15 years.

Such connectedness—hooking up suppliers, stores, staff and even banks—is the sort of thing that most retailers can still only dream of, even with the Internet around to reduce the cost and the complexity. What made Seven-Eleven's task more daunting was that the system had to serve some 6,000 stores (the figure is now more than 8,500 and growing) scattered across Japan.

It built the system itself, creating the hardware with NEC, a consumer-electronics company. Coming up with the right software was harder, and it eventually asked Microsoft, America's software giant, to help it build a tailor-made Windows-based system.

By 1996 the software was being installed in some 61,000 computers at Seven-Eleven's stores, head office and vendor firms. By 1998, the overhaul, which cost ¥60 billion ($490m), was complete. The new system replaced the ragbag of systems used before. A pipeline to Microsoft's offices in Seattle provided instant support. The software back-up constantly monitored and automatically rebooted the system when it crashed, and alerted local maintenance firms if such errors occurred more than twice.

All Seven-Eleven stores now have a satellite dish. Cheaper than using ground cables, this is often the only option for shops in rural areas. And in earthquake-prone Japan, the satellite dish provides an extra layer of safety on top of two sets of telephone lines, and separate mainframes in Tokyo and Osaka.

Win-win-win-win

Seven-Eleven's new technology gave it four advantages. The first was in monitoring customer needs, which were changing as deregulation made shoppers more demanding. "We believed that the nature of competition was changing. Instead of pushing products on to customers, companies were being pulled by customer needs. In this environment, the battleground was at the stores themselves—the interface between businesses and customers," says Makoto Usui, who heads the information-systems department at Seven-Eleven.

Second, Seven-Eleven uses sales data and software to improve quality control, pricing and product development. Thanks to its systems, the company can collect sales information from all its stores three times a day, and analyse it in roughly 20 minutes.

This has helped it rapidly to discern which goods or packaging appeal to customers. "Seven-Eleven's merchandising and product-development capabilities are formidable. Its ability to sense new trends and churn out high-quality items is far superior to other operators," says Michael Jacobs, an analyst at Dresdner Kleinwort Wasserstein, an investment bank. Now Seven-Eleven is using these skills to increase its own-brand products, which have higher profit margins.

Third, technology has helped to predict daily trends. As customers become more fickle, product cycles are shortening. Fashions in boxed lunches, riceballs and sandwiches, which make up almost half of a convenience store's daily sales, are especially short-term. Most last about seven weeks, but they can be even shorter.

Seven-Eleven says it can keep abreast of these partly by keeping an eye on the weather. Five reports a day arrive electronically at its stores from hundreds of private weather centres, each covering a radius of 20km (13 miles). This is useful in Japan, where temperatures between towns 40km apart can vary by as much as 5°C. The reports also compare today's temperature with yesterday's. "The same 10°C can feel very different depending on whether it was 1°C or 20°C the day before. This is critical for predicting food purchases," points out Mr Usui.

Finally, Seven-Eleven's electronic investment has also improved the efficiency of its supply chain. Orders flow quickly. Those sent in by 10am, for delivery after 4pm, are electronically processed in less than seven minutes. They are sent to 230 distribution centres that work exclusively for Seven-Eleven. Truck drivers carry cards with bar codes that are scanned into store computers when they arrive with a delivery. If a driver is often late, the operator will review his route and might add another truck to lighten the load. Seven-Eleven folk boast that their trucks run even more punctually than Japan's on-time buses.

In the same way, Seven-Eleven also helps vendors and manufacturers to control their inventories. It

uses its database to instruct them on all sorts of small details, such as what sauce to put into its ready-made noodles in order to maximise sales.

As well as the system that links together its supply chain, Seven-Eleven has worked hard to use technology to improve communications and training. Multimedia tools have helped to train store attendants, always a difficult task for a business with lots of stores and part-time workers. Technology has also provided a way for store workers to keep in touch. That is important in a business which runs round the clock, with stores manned by a dozen or so workers, some of whom never see each other.

What about the Internet?

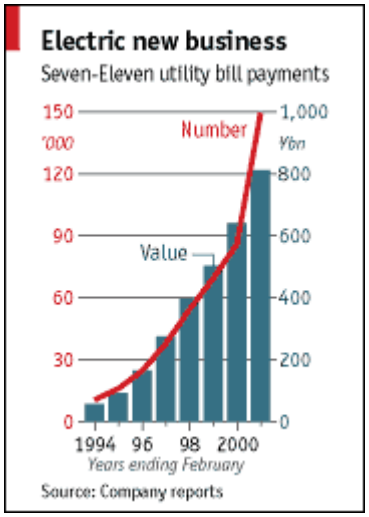
If Seven-Eleven had built its new system three or four years later, would it have based it around the Internet? The company says that, even if it were developing a similar system today, it would not necessarily use the Internet for all its operations. It prefers the security of a proprietary network. And some of the advantages of an Internet-based network for American and European companies are less apparent in a Japanese context, where supplier relationships tend to be deeper and more stable. Seven-Eleven sees no virtue in allowing new Japanese suppliers to put in bids over the Internet.

It is, however, hedging its bets by studying how international rivals such as Wal-Mart use the Internet for global product procurement. And it will watch closely what happens at Lawson, which together with Mitsubishi Corporation, the biggest trading house, is building a replica of Seven-Eleven's system based on the Internet.

Seven-Eleven is already using the Internet to lower its annual overhead costs of around ¥70 billion. It plans to install an e-commerce software package offered by the Japanese arm of Ariba, an American e-procurement company, to bulk-buy goods and services such as office equipment and insurance policies for its employees.

The big question is whether Seven-Eleven can integrate the Internet into its other operations. In the past, it has been clever at finding new ways to use its technology. Back in 1987, after installing bar-code recognition systems, Seven-Eleven turned its stores into payment points for utility bills. Almost 15 years later, the move (which required only a small incremental investment in software) has given Seven-Eleven 3% of a massive market that includes big rivals such as banks and post offices (see chart).

Now the company has increased its customer traffic by turning shops into payment and pick-up points for Internet shoppers. This was a clever move in a country in which people are still wary of using credit cards over the Internet, preferring instead to pay cash at a store. Most customers at e-Shopping!Books, an online bookseller, pick up and pay for their purchases at a Seven-Eleven store. Indeed, says Seven-Eleven, some 75% of Internet shoppers pick up their purchases from bricks-and-mortar stores.



Thanks in part to such tactics, Seven-Eleven's stores now sell almost 50% more on average every day than those of its closest rival. Whether its latest projects will be as successful has yet to be seen. Its Internet site, 7dream.com, was launched last July with seven other companies, including NEC and Nomura Research Institute. The site offers a wide range of goods and services, including books, CDs, concert tickets and travel.

But the site's lack of focus could hurt its ability to develop specific online brands, argues Mr Jacobs. The company has already said that the heavy costs it will incur to build up 7dream.com's content mean that its consolidated pre-tax profits will not grow in the current financial year.

Seven-Eleven has also had problems with its branchless bank: IY Bank, which opened in May. The bank, officially owned by its parent company, the Ito-Yokado supermarket chain, had a struggle to win approval from the authorities (it was the first non-bank to apply for a banking licence). It is also expected to have a tough time meeting the strict profit targets set out by the Financial Services Agency.

When it comes to running such online businesses, Seven-Eleven seems likely to have just as much difficulty as others have done: lots of costs, few customers. For the convenience store, as for other businesses, the real savings are likely to come from deploying the Internet as a management tool. It

already knows how to cut costs by replacing paper with electronic delivery: it has trimmed ¥300m a year over the past decade by becoming a “paperless” business. Now it wants to save more.

To do this, however, it will have to answer two more big questions. First, can it integrate the Internet into its elaborate proprietary network? Seven-Eleven’s managers think it can: indeed, they claim to have designed such potential for flexibility into the existing system. But an investment designed with a 15-year life may be a big psychological barrier to seeing the Internet’s strengths.

Secondly, is Seven-Eleven willing to use technology to cut costs? The company says—as do many others—that human capital, augmented by technology, stands at the centre of its business. Like most Japanese companies, it insists it does not use technology to lower staff count. The point is to improve service, not cut staff.

However, only by using technology to expand markets or to reduce staff can a company earn back the cost of such an investment. So far, Seven-Eleven has found ingenious ways to expand its markets. If that were to stop, it might find it needed less human capital than it has now.

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Low-cost airlines

The squeeze on Europe's air fares

May 24th 2001 | LOVE FIELD, TEXAS, AND LUTON, ENGLAND
From The Economist print edition

Low-fare, no-frills airlines are shaking up Europe's national flag carriers

Get article background

ANY day now, British Airways (BA) should complete the sale of its low-fare subsidiary, called Go, to a management buy-out backed by capital from 3i, a venture-capital group, and Barclays Bank. It will launch on to the market an aggressive competitor in what has become the hottest sector of European aviation.

Europe's two leading low-fare carriers, Ryanair and EasyJet, are not only expanding their route networks out of Britain, but also setting up bases in continental Europe, where low-fare airlines are few and far between. For an increasing number of passengers in Europe there is now an alternative to the sky-high fares charged by national flag carriers. This week, a round-trip traveller from London to Frankfurt could choose between paying £500 ($714) for an economy return on BA or Lufthansa, or just over £200 on Ryanair.

Low-fare airlines emerged from the deregulation of Europe's skies that came into full effect in 1997. Any qualified airline can now fly anywhere within the European Union, without any need for government approval. With this liberalisation came the first widespread competition for national flag carriers, then still mostly state-owned. Previously only BA had had much competition (from British Midland and Virgin Atlantic). Then Ryanair and EasyJet took off.

Low-fare, no-frills airlines such as these are modelled on Southwest Airlines, a Texas-based carrier that was the first to exploit successfully the deregulation of America's skies in 1978. Southwest's no-frills business model famously involves no free meals or coffee, only peanuts. But fares start at around one-fifth of those of the mainstream carriers. It operates short, point-to-point flights between secondary airports, sometimes over an hour's drive from city centres. And it has a fleet made up entirely of one type of aircraft, the Boeing 737, to keep down costs.

Labour is cheaper than in the big airlines and cabin crews do the cleaning, speeding up turnaround times to 20 minutes and allowing aircraft to be used for 15 hours a day. That is twice as much as in a conventional airline that runs a hub-and-spoke network, in which aircraft must wait to connect with waves of incoming and outgoing flights. The Southwest way can bring costs down to half those of a mainstream airline.

Southwest now has the eighth-largest fleet of any airline in the world (bigger than BA's or Lufthansa's), and it challenges the mainstream airlines in America in the number of passengers carried on its national network. As American takes over TWA, and United attempts to swallow US Airways (a deal that still awaits antitrust approval), the "Southwest effect" is being cited as a counterweight to the concentration of market power in the hands of the big airlines.

When a low-cost carrier enters a market, its bigger rivals are forced to cut their fares. After JetBlue started flights last year between New York's JFK airport and Buffalo, with a low fare of $47, traffic rose by 54% and average fares fell by 20% as other carriers were forced to respond.

European imitations

The Europeans have copied Southwest, and the closest imitator, Ryanair, is even more profitable than the Texan airline (see table). As one Southwest manager said recently, "Thank God these guys are not allowed to operate in the United States."

Ryanair specialises, like Southwest, in using secondary airports, where it is paid to land because of the trade it brings, rather than having to bear the stiff landing charges of the big hubs. So a Ryanair flight to Paris lands in Beauvais, about 80km north of the French capital. There it meets a connecting bus to the city centre.

The Southwest gang
Low-cost airlines

	Southwest	Ryanair	EasyJet
Aircraft	332	31	18
Routes	280	43	28
Daily departures	2,548	217	144
Profit margin, %*	18.0	24.3	8.3

*Pre-tax, latest financial year

Sources: Schroder Salomon Smith Barney; J.P. Morgan

EasyJet is Ryanair's biggest competitor, flying to airports around Europe from Luton and Gatwick airports near London. While Ryanair grows by adding extra routes, EasyJet expands by increasing the frequency of its flights, which means that it attracts cost-conscious business travellers on routes to places such as Glasgow, Edinburgh and Barcelona. Although it already has a presence on the continent (with bases in Geneva and Amsterdam) it sticks to the Southwest formula of not scheduling connecting services.

Like other low-fare carriers, EasyJet has a flexible pricing policy that rewards those who book early and charges top whack for those who come along at the last minute. It also benefits from those who fail to turn up for a flight. Unlike latecomers on mainstream airlines, they get no refund, allowing EasyJet sometimes to sell their seat again to a last-minute arrival. EasyJet also now has the highest share of online bookings anywhere in the industry, at over 90%. That compares with around 60% for other European low-fare carriers and just over 30% for Southwest.

Not all Europe's low-fare carriers, however, have been a success. Virgin Express—Euro-Belgian Airlines before it was bought by Sir Richard Branson—has never done as well as the others. It was not as focused as the best and has been cutting its services to stem losses. Another low-fare carrier, Debonair, went bankrupt after only a couple of years. It used expensive-to-run aircraft and had a confusing brand image, being neither straightforwardly low-fare nor a full with-frills competitor.

Where are the others?

One of the puzzling aspects of the spread of British-based low-cost carriers across Europe is that they should have been left with the skies much to themselves. There may be a natural tendency for the British and the Irish to latch on more quickly to American ways. The early Ryanair traffic was based on fare-conscious Irish folk visiting friends and relatives, the so-called "VFR segment" that has always been the bedrock of Southwest's market. The Irish expatriate population in London provided a strong launching-pad before Ryanair's boss, Michael O'Leary, applied the formula more widely.

High social costs are a hurdle for low-fare, low-cost carriers in continental Europe, although both Ryanair and EasyJet are confident enough now to run continental bases with local staff. A bigger obstacle is the competition provided by intercity trains. High-speed rail travel is cheap and efficient in France, Germany and Italy.

Even where rivals to flag carriers have set up in continental Europe, they have been content to be "me-too" operations, carving a niche by offering conventional with-frills services at a slightly lower price. One example is Air One in Italy, which offers gentle competition to Alitalia on domestic routes. Another, Air Liberté in France, soon came to grief. It ended up first under the wing of BA, then of the Swissair group. But Swissair is now backing out because of its heavy losses.

This week, the boss of Air Liberté, Marc Rochet, unveiled a recovery plan which involves cutting services and running feeder flights to connect with long-haul Air France routes. It looks less like a low-fare

strategy than an attempt to creep under the wing of yet another flag carrier.

Until five years ago, cheap air travel in Europe was restricted to charter flights in holiday packages. Charters still account for about half of all intra-European flights. But low-fare carriers offer people the opportunity to design their own packages, often providing access to cheap car hire and accommodation as well through their websites. Today, low-fare flights account for only about 3% of scheduled traffic in Europe, compared with 22% in America. But since the low-fare airlines are growing by 25% a year and forcing their bigger rivals to cut their loss-making European routes, it will not be long before the protected economics of Europe's flag carriers are undermined. That, in turn, may help to bring about their long-overdue consolidation.

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Europe's big airlines

On merger stand-by

May 24th 2001
From The Economist print edition

Mixed results from Europe's airlines mean consolidation is overdue

BRITISH AIRWAYS and KLM in recovery; Air France booming as ever; once-proud Lufthansa sliding badly; and Swissair struggling to survive. Europe's national flag carriers present a mixed picture. But they are all feeling pressure from the low-fare start-ups that are upsetting the cosy world of European air travel (see article).

The European Union has 14 big airlines. America has six, which are about to consolidate into three or four. The reason Europe continues to have so many is because of their status as "national champions", which means that one carrier per country is designated to exploit the international traffic rights defined in bilateral air-service agreements, the archaic treaties that separate aviation from normal business.

The first airline to get the message about the new competitive environment was British Airways. A couple of years ago, it decided that the answer was to trim its capacity so that there was no need to fill seats with the bums of backpackers on cheap deals. It was losing £300m a year in Europe, so it cut back its network there, partly under pressure from low-fare competitors. This week it reported the fruits of that strategy: a quadrupling of its operating profit to £380m ($562m).

Air France is expected to announce booming figures next week, helped by its alliance with America's Delta Airlines, which means it is able to build Paris's Charles de Gaulle airport into a big European hub serving lots of American destinations. So strong has Air France become that it is now seen as the saviour of Alitalia. The Italian carrier tried to merge with KLM, but the deal fell through last year. It desperately needs an alliance because its Milan hub is dysfunctional and it wants to tap into markets beyond northern Italy. This week both airlines confirmed that they were talking about what they call "Project Albatross".

Paradoxically, the only European alliance actually to happen, Swissair's purchase of a 49% stake in Belgium's Sabena, did indeed turn out to be an albatross: an unwanted burden around the neck of the Swiss carrier as it ran into problems of its own. So that deal is being unscrambled. But it is merely a distraction from the underlying trend towards consolidation around Europe.

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French investment abroad

Behind the bluster

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From The Economist print edition

Anti-globalisation in France is more appearance than reality

IT WAS more than a symbolic defeat: on May 16th, Robert Mondavi, a big Californian wine maker, announced that it had abandoned plans to build a winery in Aniane, a small village in France's Languedoc region. The recently elected mayor of Aniane had denounced Mondavi's plan, which had been approved under the previous mayor, as a capitalist plot designed to benefit shareholders rather than locals and the environment. In March, demonstrators had smashed toll-booths and fought with police in protest. Mondavi pulled out, citing personal and political interests that it did not understand.

The episode was reminiscent of the anti-globalisation campaign led last year by José Bové, a one-time nuclear protester turned small farmer who became famous for his protests against McDonalds. It also echoed the recent fuss over Marks and Spencer, a British retailer that has been attacked for shutting its French stores, with the loss of 1,700 jobs. But such well-publicised behaviour disguises the truth, which is that French companies are quietly furthering their own globalisation, even as they noisily defend their home turf.

Mondavi's defeat coincided with a rush of controversy generated by French companies seeking to increase their presence abroad. On May 18th, it emerged that Alcatel, a big French telecoms-equipment group, had reopened multi-billion dollar merger talks with Lucent, a struggling American rival. Three days later, Vivendi Universal, a media group based in France, announced that it had offered to buy MP3.com, an American online music-sharing company; and on the following day, Vivendi did not deny that it was in the early stages of negotiating to buy Houghton Mifflin, an American publisher that could be worth around $1.7 billion. Such a flurry of Franco-American deals is unprecedented in recent years.

Meanwhile, state-owned Electricité de France (EDF) has become mired in ugly battles in both Spain and Italy. At the start of May, the Spanish government suspended the voting rights of two foreign companies that had bought shares in a small utility. One of those companies is controlled by EDF. The Spanish accuse the French of double standards on market opening and are considering whether to restrict voting rights so that EDF is held at bay.

The Italian fight is even dirtier. It arose after EDF took a 4% stake in Montedison, a holding company that is under pressure to break itself up and put into play Edison, Italy's second-largest electric utility. Italians have expressed outrage that a protected foreign state monopolist is butting into their electricity market. The government is even toying with imposing legal curbs on foreign state-owned companies' investment. Unabashed by the fuss, EDF has blithely raised its stake to more than 20%.

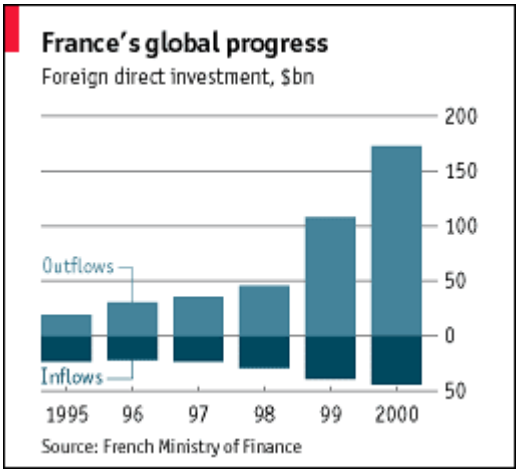
Yet a picture of French companies bestriding the globe while refusing to allow competitors into France is altogether misleading. Levels of foreign direct investment (FDI) into France have never been higher. Last year, for example, France recorded 563 inward investment deals, up from 447 in 1999. America accounted for 178 of them, with Germany the second-biggest investor with 102. More than 35,000 new jobs will be created over the next three years by such investments.

Longer-term figures from the OECD tell a similar story. In the late 1980s, France invested nearly twice as much overseas as it received from abroad. Until 1998, the gap remained much the same. Although the trend appeared to go into reverse in 1999 and last year, this can be explained largely by the effect of a few huge deals, notably Vivendi's $34 billion acquisition last June of Seagram's Universal business.

This is consistent with other measures. Research by J.P. Morgan on global mergers and acquisitions suggests that activity by

French companies is in line with the size and influence of the French economy. European companies in general have been big buyers of their North American counterparts, snapping up $1.16 trillion-worth of assets there since 1988. Britain has been by far the biggest acquirer, with $504 billion-worth. France's $186 billion places it a distant second.

EDF's belligerence and Mondavi's retreat, it seems, are exceptions to the broader trend of France's active participation in the globalisation game. But the episodes carry a warning nonetheless. France has its sacred cows—nuclear power and gastronomy among them. It also has a populace that has, for over two centuries, never been slow to take to the streets. Foreigners wanting to enter the French market should pick their targets with a careful eye towards national sensitivities.



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Face value

Blandishments

May 24th 2001
From The Economist print edition

BT's new chairman, Sir Christopher Bland, has the job of putting the ailing telecoms giant back on line

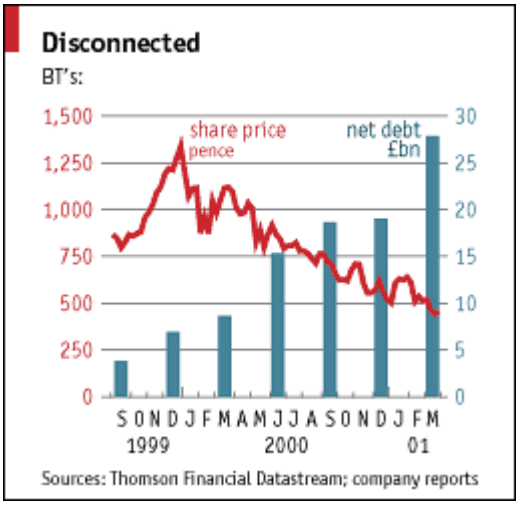
LARGE, jovial and energetic, Sir Christopher Bland clearly cannot abide a mess. Before he sits down in his calm room at Broadcasting House, right in the prow of the BBC's ocean-liner of a building in London's Portland Place, he spots a tulip wilting in a vase. "Away for a day and things fall apart," he says crossly, whisking it out and into the bin.

Dead flowers are one consequence of dividing his time between chairing the board of governors of the BBC, Britain's state-owned broadcaster, and of BT, the former state-owned telecommunications business whose chairman he became at the start of May. He has chaired the BBC since 1996, and had two more years to go when he got a call from a headhunter, asking whether he would ever consider leaving the "Beeb". "No," he said, "except for BT."

BT it was. He got the job after being interviewed by Sir Iain Vallance, the outgoing chairman, Lord Marshall, a non-executive director, and Sir Peter Bonfield, the chief executive. He rejected the idea of joining first as a non-executive and then taking over as chairman in the autumn. However, he agreed to continue the BBC job until the British general election (on June 7th) is out of the way, so as to spare this government the sensitive task of choosing his successor.

At BT, things have been falling apart recently. Over the past year the company's shares have collapsed (as, to be fair, have those of many other telecoms companies). And its debt has soared, to £27.9 billion ($40 billion), leading to a £5.9 billion rights issue, the biggest-ever in London. The issue is now being promoted heavily to investors, who remain unhappy—BT's shares have fallen in value by 10% since it was announced, and they were pushed down further this week by two high-level resignations from Viag Interkom, BT's German mobile-phone subsidiary. Sir Iain's departure was the smallest price that investors would accept in return for helping the company out of its mess.

Sir Christopher's qualifications for the job are some familiarity with the fast-changing world of communications; plenty of experience of dealing with regulators; and the cheerful thuggishness of a man who once fenced for Ireland in the Olympics and spent his 20s as a Territorial Army (part-time) soldier.



His acquaintance with the digital world comes from the BBC, where he presided (admittedly from a great height) over the development of one of Britain's most popular websites. His experience of dealing with regulators is far broader. He was chairman for 15 years of a large group of hospitals ("that's why I'm a Sir and not a plain Mr"); chairman of London Weekend Television for a decade until 1994; and chairman of NFC (the remnants of a state-owned road-freight service) until May 2000.

As owner of the local "loop" connecting homes to the national network, and as provider of the bulk of Britain's domestic telephone services, BT is bound by tight rules. A good understanding of regulators is therefore a valuable skill for its chairman. So is an ability to deal with politicians. Sir Christopher is proud that, on his watch, the BBC negotiated good deals with the government on the licence fee that finances it and on the special provision to cover its World Service.

But thuggishness may turn out to be his key quality. He will need it first to sort out BT's finances. He spent much of April wading into the task of reducing the debt. His priority is to get it down to between £15 billion and £20 billion. With some £6 billion from the rights issue, around £5 billion from various disposals, and £1.5 billion-3 billion from a sale or flotation of Yell, the company's Yellow Pages business, that target starts to look feasible. To help to meet it, the company is cutting its dividend ("It makes no sense to say, we need £5.9 billion, and here's £1.4 billion back"). It must also unscramble the complex deal that binds BT to AT&T in Concert, a blighted and hugely loss-making international venture.

In all of this, Sir Christopher has already been vigorously involved. "I used April to do quite a lot of due diligence on the current strategy of the company," he recalls, "and the choice was pretty clear. Either I bought into it—or I didn't come." He did not have the luxury of looking at alternatives. So he chaired the board that decided to cut the dividend, and he was involved in the delicate task of setting the terms of the crucial rights issue.

Beyond that lies the task of splitting BT into two parts, dubbed BT Wireless and Future BT. The need for a split, some would say, was obvious long ago: but Sir Christopher firmly refuses to luxuriate in hindsight. He is to run the second, slower-growing bit. "I quite like businesses that generate cash earnings and have a dividend-paying potential," he says cheerfully. "I'm an old-economy person."

The Bonfield business

Sir Christopher has invested £1m of his own money in BT, so he clearly thinks he can make the transition work. But it will need a change in BT's stilted and bureaucratic culture. Changing the culture is something he believes is being done by Greg Dyke, the director-general appointed to the BBC under his chairmanship. But BT had a succession of problematic chief executives under Sir Iain, and Sir Peter has stayed longer than anyone since Sir Iain himself did the job.Can the company's culture be changed so long as Sir Peter, whom many outsiders blame most for the current mess, remains in the job?

Sir Christopher, for once true to his name, smiles blandly. "It's a question he and I need to answer together. We think we can." Clearly, no company willingly dumps both chairman and chief executive at the same time. When BT splits, that may be the time for Sir Peter to split too. The biggest test for Sir Christopher is likely to be not how well he gets on with Sir Peter, but how successfully he picks Sir Peter's successor.

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Interactive TV

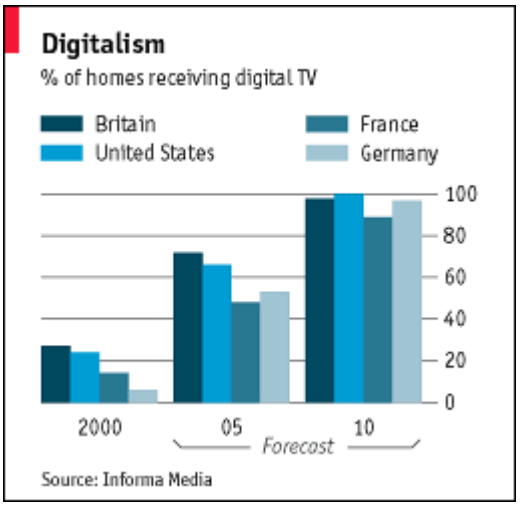
How to skin a potato

May 24th 2001
From The Economist print edition

It is proving hard to make money out of interactive television

WHEN BSkyB, a British satellite-television broadcaster owned by Rupert Murdoch's News Corporation, pulls the plug on its old-fashioned analogue service this summer and becomes a digital-only provider, it will be the world's first nationwide analogue broadcaster to make the switch. Thanks mainly to the decision by BSkyB and rival British cable companies to give away the set-top boxes through which their channels are received, digital television is now pumped into no fewer than 27% of British homes, a greater share than in America (see chart). And, this figure is expected to leap to 72% by 2005.

Digital brings many features, among them a clearer picture and the ability to squeeze more channels into the box. But the main reason why British pay-TV broadcasters, with their continental counterparts, are in breathless pursuit of this costly conversion is that digital TV promises interactivity: the ability of viewers to "talk" to the telly. Interactive TV, it is said, will animate couch potatoes, tempting them to spend money ordering anything from pizzas to package holidays, all at the press of a remote-control button. Jupiter Media Metrix, a research firm, has forecast that, by 2004, revenues from interactive commerce and advertising will have risen to $8.1 billion in Europe, and to $5 billion in America.



There are reasons for their optimism. Compared with the PC, the television is a friendly antique, a piece of living-room furniture familiar even to technophobes. The vast majority of Europeans already have a television set in their homes, but less than a third are wired to the Internet. On average, they sit in front of a television for about eight times as long as they sit in front of a computer.

Yet interactive TV is a fledgling creature, and its bosses are still trying to work out quite what it is for. Europe's experiment so far suggests one conclusion: it is simpler to persuade digital viewers to try out snazzy interactive services than it is to make them spend money.

The most disappointing use of interactivity has been for shopping, or "t-commerce". Earlier this month, BSkyB announced that it was folding its interactive-shopping channel into the group's general interactive division. Called Open, the channel was launched with great fanfare in 1999. But by the end of last year, when 4.7m of BSkyB's 5m subscribers had digital interactive television, only 500,000 of them had actually bought anything.

Although BSkyB will not say as much, its decision to fold Open into its general interactive division may mark a U-turn in thinking about how to sell interactively on the box. Open exemplifies what the industry calls the "walled garden" model: a sort of mini-shopping mall on television. Not only does the viewer have to be lured to the channel, but, once there, he has less information available than he would on the Internet. Retailers grumble about the high rents charged for a plot in the walled garden and the cost of setting up the technology: television operators use different, and incompatible, operating systems inside the set-top box.

The fashionable idea now is to sell "in the broadcasting stream": that is, to try to distract shoppers as they watch a popular music show, say, by getting them to click to buy the latest compact disc. Sell the viewer something that relates to what he is already watching, goes the argument. While the technology now exists to make this type of selling work, it remains uncertain whether viewers glued to a favourite soap will want to interrupt it in order to buy the soap star's shoes.

So how is value to be extracted from interactive TV? One innovative approach is in sport. In June, for instance, the BBC will offer subscribers to digital satellite services interactive coverage of the Wimbledon tennis tournament. This will allow viewers to select any one of five live matches, or to watch five at a time on a split screen. In the short run, this sort of feature may help boost ratings, discourage people from cancelling subscriptions, and draw advertisers to any one channel. But if all the broadcasters end up doing the same, there may be no net revenue gain.

Does any interactive application make extra money from viewers? One item repeatedly mentioned is pizza. But, as Theresa Wise of Accenture, a consultancy, puts it: “You can’t build an entire economic model based on the sale of pizzas.” The real answer turns out to be betting and games. BSkyB, for instance, revealed this month that out of £60.2m ($86.7m) of interactive revenues in the nine months to March this year, no less than £55m came from betting.

Games also seem promising. A broadcaster will charge viewers each time they play, and add it to their monthly pay-TV bill. Games can be played either on dedicated games channels, or while the viewer is watching a programme. The latter, known as “enhanced television”, is beginning to get interactive television people excited. The idea is to add an interactive game to an ordinary programme, something that seems to work best with quiz shows and sport.

In trials conducted by Two Way TV, a British interactive-TV company, ratings jumped by an average of 30% in peak time, and more than doubled in the daytime. To play a typical game, during a live football match, the viewer sits with his finger on the remote control, guessing the outcome of each move: will the striker score from a penalty? Will the corner end in a goal? He can play against friends at home, or others also playing live. The highest scorer wins the jackpot. Two Way has just devised an interactive game for the new British series of *Big Brother* (see article).

Even if games and betting take off, however, it will be some time before broadcasters can make interactive television pay for their investment in digital. This month, BSkyB reported that pre-tax losses for the nine months to March this year had jumped from £89.9m to £365.3m, its third successive year of losses—thanks chiefly to the massive cost of converting to digital.

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Reality TV

Antics in the attic

May 24th 2001
From The Economist print edition

Europe is learning how to sell tacky TV to the Americans

WHILE Europeans grumble about the degrading impact of American cultural imperialism, they are quietly getting their own back by selling the Americans hours and hours of tawdry voyeurism in the shape of so-called “reality” television. Reality TV puts groups of volunteers in unreal situations—on a desert island, for example, or locked up in a loft. It then subjects them to constant surveillance by camera and forces them to play humiliating games which often encourage them to take their clothes off—all with the promise of a handsome prize for the winner.

“Big Brother”, now stirring huge controversy in France, where it is called “Loft Story”, is a prime example. Screened on a hitherto minor channel, M6, “Loft Story” has lured a massive 50% of all French viewers on some days. Scandalised, the French audio-visual authority has ruled that the show fails to “respect the dignity of the human being”, and that contestants must get a daily break from the cameras.

Many of these shows have been hits in America, but almost all were dreamed up by Europeans. “Survivor”, for instance, which was a massive hit on CBS last year, drawing an astonishing 51m viewers to its final episode, arrived in Britain only this week. But Charlie Parsons, its creator (and the holder of its “format rights”), is British. “Big Brother”, which was also picked up last year by CBS and runs for a second series this summer, was created by a Dutch company, Endemol, which produces the show in 17 countries worldwide. Endemol also created “Chains of Love”, now showing on UPN, in which couples are chained together 24 hours a day.

Such is the apparent American appetite for these shows that the networks, faced with the escalating fees charged by comedy stars, have been nudging out the traditional prime-time fare of sitcoms and dramas in their favour. This autumn, the schedules on all four big networks are packed with “reality” TV shows and other European exports.

European creators are working on scores of new formats, hoping to devise the next blockbuster. A format holder can expect to earn a 5% royalty on each series commissioned, or an average of perhaps $2.5m. Revenues at Endemol, the most successful exporter of game-show formats, jumped by over 50% in the first quarter this year. Last year, it was bought by Telefonica, a Spanish telecoms firm, for a mighty *euro*5.5 billion—a handsome prize for Endemol’s investors that required neither their humiliation nor their nakedness.

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Hair dye

Fast-growing business

May 24th 2001 | NEW YORK
From The Economist print edition

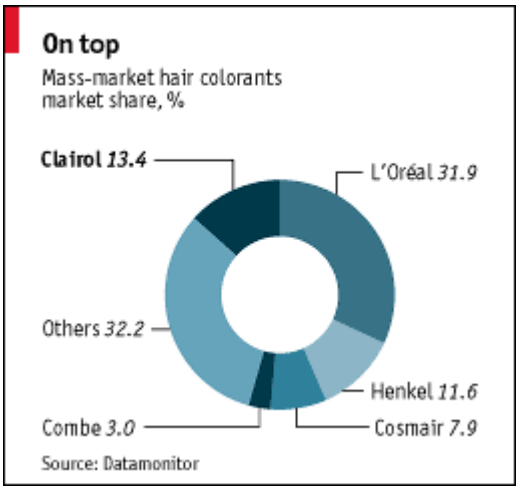
Procter & Gamble's $5 billion purchase of Clairol is not without its risks

EPA

Hair today, dyed tomorrow

WHEN it comes to the colour of hair, grey is definitely not the new black. From fusty American baby boomers to funky Japanese teenagers, more and more women—and increasingly men—are buying boxes of hair dye, donning rubber gloves and trying not to splash the bathroom floor with coloured glop. The global market for hair colorants, already worth an annual $7 billion in retail sales, is expected to grow by 8-10% a year over the next five years. That makes it by far the fastest-expanding segment of the $37 billion hair-care industry.

A desire to tap into that growth has prompted Procter & Gamble, a household-goods giant, to pay $5 billion in cash to buy Clairol from Bristol-Myers Squibb, a drug maker. P&G is already big in more mature bits of the business such as shampoos and hair spray (which Clairol also sells). The attraction of this deal is Clairol's 13.4% world market share in colorants, which is second only to that of L'Oréal (see chart).



Two things are fuelling the popularity of dyes. The first is the wish of ageing populations everywhere to cover their grey. "Being 50 today is not like being 50 ten years ago," says Debra Leitman-Yale, president of Clairol International. "Women are fighting ageing every step of the way." Half of all women in America and Europe already colour their hair regularly, and this percentage is rising as baby boomers head towards retirement. And as do-it-yourself hair-dye kits become gentler on the tresses, easier to use and cheaper, half of them are now doing it at home rather than in salons.

They are being joined by more and more men. In Japan, where boys increasingly seem to want to look like girls, hair dyes (along with eyebrow tweezers) are big business. In America, sales of dyes to men tripled in one year, to $130m in 1999, according to A.C. Nielsen. Making hair-dyeing butch is part of the trick. Clairol's website advises men with thinning hair to dye it to make it look fuller, while Combe, one of its rivals, uses football stars to push its popular Just for Men range. Even Tiger Woods, it seems, has dyed his hair.

The second factor is the explosive popularity of hair colour as a fashion accessory, particularly among the young. Yiotis, the creative director of colour at Vidal Sassoon London, who personally tints the locks of Oscar nominees and catwalk models, says: "In the past, people would carry a Prada bag or wear Gucci shoes. Now the latest accessory is dyed hair." Clairol notes that the fastest growth is coming from people aged between 14 and 24, where the prime objective is to be noticed.

One factor helping sales is that the new dyes are not so fast, allowing frequent colour changes and experimentation. In Japan, where so many cutting-edge trends start, hairdressers have acquired celebrity status: female students there recently rated hairdressing as "the job with the most imaginative appeal".

Although P&G may be able to strengthen its new brand's global distribution and save some costs, Clairol has been losing market share in America, largely to L'Oréal. Figures from IRI, an American research firm, show that since 1995 Clairol's share has slipped from 49% to 37%; L'Oréal's has jumped from 34% to

41%. In Europe, meanwhile, Germany's Wella, which announced good results this week, and Schwarzkopf (made by Henkel) are well entrenched.

Like that other fashion accessory, the mobile phone, hair dye is starting to come with a health warning. A recent report in the *International Journal of Cancer* found a link between hair dyes and bladder cancer. In Britain this month a woman died from an allergic reaction after colouring her hair at home. Smelly chemicals that help hair absorb colour can also cause odd reactions. Experts are even recommending drinking a litre of water after dyeing in order to dilute any peroxide absorbed through the skin. Such concerns will probably not deter the vain, though. After all, suffering in the name of beauty is an age-old tradition.

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Ford and Firestone

Screeching to a halt

May 24th 2001 | DETROIT
From The Economist print edition

Last year's tyre crisis has returned to haunt Ford and Firestone

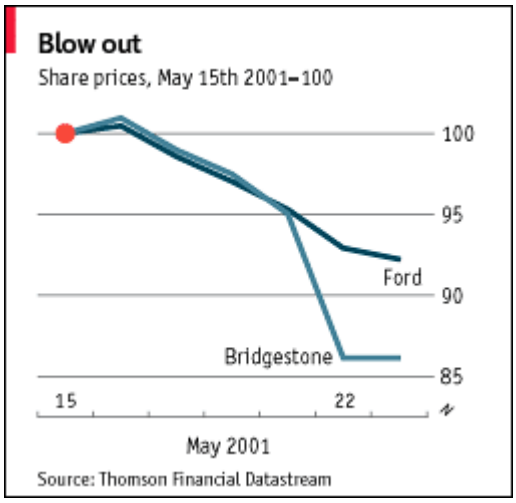
THERE is more to Ford's recall of Firestone tyres this week than meets the eye. The latest skirmish in the increasingly bitter war between the two companies is over nothing less than the fate of the car maker's most profitable products. That is why Ford, without any federal prompting, is ready to spend up to $3 billion to recall and replace 13m Firestone Wilderness AT tyres, most of them used on its popular Explorer sport-utility vehicles (SUVs). That is twice as many as in an earlier recall last summer, triggered by the deaths of at least 170 American motorists.

AP

The nature of the problem

First indications suggested that several versions of the Wilderness tyre involved in the earlier recall, and particularly those produced at an Illinois plant with labour problems, were prone to suffer catastrophic tread separation, leading to a loss of control and often a fatal rollover accident. By comparison, the tyres involved in the latest recall are far less likely to blow out, Ford admitted on May 22nd. But, stressing that he "lacked confidence in Firestone", Ford's chief executive, Jacques Nasser, said at a news conference that he ordered the recall anyway because of increasingly disconcerting data. As the tyres aged and logged more miles, they "were sending out warning signals about future problems."

Firestone officials wasted no time in insisting that the real problem was Ford. In a pre-emptive strike, the tyre maker offered its own trend data—but no hard proof—suggesting that the Explorer at least contributed to the high rate of blow-outs. At a meeting with Ford on May 21st, Firestone's boss John Lampe made clear that his company would not participate in the latest recall. Indeed, it would no longer work with Ford at all. Wrapping up the meeting, he handed over a letter for Mr Nasser which stated: "We believe you are attempting to divert scrutiny of your vehicle by casting doubt on the quality of Firestone tyres." The tyre maker, the letter concluded, would no longer supply Ford.



With that, one of the longest marriages in automotive history came to an end. It began in 1896, when Henry Ford I turned to Harvey Firestone for tyres for his experimental quadricycle. A decade later, the fledgling Ford Motor Company again turned to Firestone, which became the car maker's largest supplier for much of the 20th century. The link became even closer. William Clay Ford Jr, chairman of the car company, is the great-grandson both of the original Henry Ford and, on his mother's side, of Harvey Firestone.

Most of the tyres recalled last year were produced in Decatur, Illinois, at a time when the plant was relying on scab labour during an industrial dispute. Many of the tyres now being recalled were also produced in Decatur. Even so, nobody seems able to explain why Firestone tyres have had so many problems when used on Ford's light trucks but not when used on other makers'.

The car company rejected Firestone's suggestion that the cause lies at least partly with the Explorer. From 1997 to 2000, Ford split its orders between Firestone and Goodyear, each supplying 2.9m tyres. There were 1,183 reports of tread separations involving Wilderness AT tyres, but only two involving Goodyear tyres, according to John Rinamaki, a senior official in Ford's North American business.

Getting that message across is crucial for Ford, which has been downright brutal in its dealings with Firestone since the tyre fiasco began last summer. It has repeatedly gone on the offensive. Normally, crisis management dictates that companies in difficulties should present a united front and act quickly. But this case was never normal. The two companies were at loggerheads within weeks of the first recall, and now Ford has acted unilaterally to head off further trouble. Just before announcing the second recall, Mr Nasser flew to Washington to brief congressional leaders, who are to hold another round of hearings on the matter early next month.

Barring a federal recall order, Firestone is likely to let Ford pick up the total cost of the recall, producing a loss for the car company in the second quarter. The recall itself will take nine months to complete, even though Ford plans to shut down three plants in the coming weeks so that extra tyres can be diverted to its dealers.

As it happens, the way that the market is slowing down, Ford probably needed to suspend production anyway. When the tyre problem first surfaced, the Explorer SUV seemed immune to any consumer backlash, but so far this year sales are down by over 23%, compared with a decline of only 9% in the overall market. The decline has continued, despite the introduction of an all-new Explorer—not even fitted with Firestones. High-margin SUVs, pick-ups and other light trucks produce most of Ford's earnings; the Explorer alone accounts for about a fifth of the total.

Ford has become a relatively small piece of Firestone's total market, about 5%. But industry analysts agree that the Japanese-owned brand is still facing an uphill fight for survival. There are reports that Firestone has problems winning orders from other manufacturers who, in the words of one industry executive, "don't see the advantage of putting tarnished goods on their products."

So far Ford seems to be outgunning Firestone, but the battle is far from over. Congressional hearings are always tricky, and public perception can hinge on a single, incriminating document or an unfortunate phrase that becomes the sound-bite on that evening's news. Meanwhile, there are plenty of lawsuits under way that could give juries the chance to weigh in with their own opinions on a technical debate that has so far stumped the experts. A Texas case comes to court in early June, providing a graphic accompaniment to the congressional hearings.

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Wall Street under scrutiny

A penny in whose pocket?

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Were investment banks crooked when they made billions of dollars from the Internet bubble?

Hulton Getty

IT ENJOYED the dotcom party as much as anyone. But now that the whole thing has ended messily, Wall Street has become everybody's favourite scapegoat. Its analysts are accused of abandoning objectivity to tout shares that their investment banks underwrote. Underwriters are said to have set the share price too low in initial public offerings (IPOs), so as to ensure a huge jump in the price when trading began. That jump in turn enabled investment banks to reward favoured clients who were allocated shares in the IPO, which clients could instantly sell at a fat profit. To compound the rascality, the banks shared in those profits by demanding return favours from the clients.

Wall Street is suddenly taking all these accusations seriously. That is in part to reassure investors that IPOs are still worth investing in, and so to help to revive a market that was once lucrative. But it is mainly out of fear of the large fines, or even jail sentences, that might result from investigations under way.

The heads of research at America's leading investment banks are now working together on a code of best practice for analysts. This is said to include severing the link between an analyst's pay and the revenues a bank earns on any deal he works on. (This practice is so deeply entrenched that it will be remarkable if such a rule ever sees the light of day.) In the same spirit, the Association of Investment Management and Research said on May 21st that it is producing a paper on "preserving" research integrity and promoting a set of "research objectivity standards". Prudential Securities has given up underwriting altogether, opting to stand or fall on the independence of its research. Admittedly, it was not a strong underwriting force to begin with.

Wall Street also faces congressional hearings in June about its conflicts of interest. It is conceivable that these could become dotcom show trials, with former gurus being accused of fleecing the public by championing the likes of Amazon and Priceline. Even scarier for investment bankers are three probes into accusations of wrongdoing in the underwriting process, along with a host of class-action lawsuits on behalf of suffering investors. These investigations—by the Securities and Exchange Commission (SEC), the regulatory arm of the National Association of Securities Dealers (NASD) and a criminal one by federal prosecutors in Manhattan—take in most of Wall Street's leading firms.

Credit Suisse First Boston (CSFB) has borne the brunt of the bad publicity. It is the only target so far of the NASD inquiry, which is further advanced than the others. Unlike the SEC, which is examining industry-wide behaviour, the NASD is (as usual) putting its energies into catching one firm, after which, precedent established, it can go after the others.

Some at CSFB say that the bank is a victim of over-zealous regulators, spurred on by competition between the NASD and the SEC. They detect an attempt to demonise Frank Quattrone, the bank's high-profile dealmaker in the technology sector. There has not, after all, been a Michael Milken for the best part of a decade. Internal inquiries at CSFB appear to have exonerated Mr Quattrone from any wrongdoing. Still, the bank has suspended two employees, for "unacceptable conduct" that supposedly broke the firm's own rules, though not the law. Some observers wonder if CSFB is preparing to wriggle off the hook by implying that any abuses were the acts of a few rogue brokers.

Sharing the shares

The main focus of the investigations is the terms under which underwriters allocated shares in IPOs. This is no simple matter. Nobody disputes that the underwriters can choose to whom they distribute shares, nor that they may favour clients that give them plenty of business. Indeed, one preoccupation of regulators is that shares in IPOs have not always been allocated in proportion to the amount of broking business a client does.

Non-binding banter often takes place with good clients, say Wall Streeters

The chief concern is about what other clients did to get an outsized allocation. Did they, for instance, hand back to the underwriter some of the profits from selling the shares, by doing a lot of commission-paying business shortly afterwards? Such commissions could be construed, in effect, as part of the underwriting fees earned by the bank. They should therefore have been disclosed. Whether this is so in law may depend on whether such kickbacks can be proved to be a binding contract, rather than a vague indication of intent. Non-binding banter—"I'll give you shares in this IPO, you take care of me later"—often takes place with good clients, say Wall Streeters.

To get shares in a hot IPO, clients may also have agreed to buy shares in future IPOs that were less exciting. Or they might have promised to buy additional shares in an IPO once trading had begun. This would have amounted to market manipulation. Innocent, plead the banks. To ask clients if they would be willing to buy in the after-market is to help learn how committed they are to the shares—not planning, in other words, to "flip" the shares as soon as trading begins.

The potential revenues from cosy arrangements between Wall Street and its friends were enormous. According to Jay Ritter, an economist at the University of Florida, official underwriting revenues were $7.3 billion in 1999-2000. But the so-called "money left on the table"—instant profits available for clients allocated shares in an IPO that soared on the first day of trading—was $66 billion. Some of that money was certainly split with the underwriters. Strangely, issuers didn't seem to mind the intentional underpricing of their IPO. A big first-day pop in their share price was viewed as a marketing success.

Seasoned regulators admit that it will be hard to prove that Wall Street firms were systematically up to no good. It will take, at the least, a lot of incriminating tapes and e-mails to prove that brokers overstepped the line between vague requests ("take care of me") and the demanding of binding promises.

Perhaps, just perhaps, the market is already reforming itself. A few IPOs are now taking place, but not with the huge first-day premiums of yore. Issuers are taking a closer look at the auction-based IPOs pioneered by W.R. Hambrecht, an investment-banking boutique in California. These act to tease out the issue price that pretty much equalises supply and demand and minimises the first-day pop—and, along with it, the opportunity for kickbacks to underwriters.

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Fidelity

A family affair

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From The Economist print edition

A new head for America's biggest fund manager

IT IS, quite literally, a trillion-dollar question: how does a fund-management operation as big as Fidelity's go about handling so much money? This is now the responsibility of a 39-year-old: Abigail Johnson, who on May 21st was named head of the fund-management arm of her family's Fidelity Investments, based in Boston, Massachusetts.

Fidelity is America's biggest money manager, with more than $900 billion in American fund business and another $100 billion in fund business abroad. On the basis of current growth rates, the firm expects the two bits of the business to be the same size within ten years. Fidelity has spent a lot on overseas expansion. It is the biggest foreign investment firm in Japan, and the biggest manager of unit trusts (mutual funds) in Britain.

Unlike competitors such as Vanguard and Barclays, which mirror stockmarket indices, Fidelity vigorously manages its share portfolios. Its investment decisions are felt in the stockmarket, and at companies in which it holds shares. Fidelity's voice is heard in the proxy motions that are filed by disgruntled investors, and in the reorganisations that follow bankruptcies. As America's biggest buyer of shares, Fidelity receives by far the largest allocation of initial public offerings. It is one of the very few investors with the clout to force the restructuring of deals that it dislikes before they come to market.

How Ms Johnson deals with these issues is still a matter for speculation. The daughter of the holding company's present chief executive, Edward Johnson (his eponymous father was the founder), Ms Johnson joined Fidelity in 1988 as a lowly analyst and quietly worked her way upwards. She ran several funds, with respectable but not stellar results, and then she became a manager of the people who managed funds.

Like her father, Ms Johnson avoids publicity. Colleagues at Fidelity say they like her for not demanding special treatment. Her lack of pretensions, no doubt, makes the nepotism of her promotion easier to swallow, particularly since her rise has been so predictable since 1995, when she became Fidelity's largest single shareholder. Her 24% stake is valued by *Forbes*, conservatively, at $10 billion. It was typical of the firm's style that the change in ownership was disclosed only in the fine print of a securities filing.

Her lack of pretensions makes the nepotism of her promotion easier to swallow

Typical, too, was that not a single word of Ms Johnson's recent promotion leaked in advance. Such secrecy would be unusual in any of the public companies Fidelity invests in. But it is one of the more curious elements of America's investment-management world that Fidelity and its most formidable competitors resist becoming public companies themselves. Vanguard, the second-largest manager in America, is mutually owned, allowing the shareholders in its funds to pay particularly low fees. Capital Group of Los Angeles, the largest fund group that sells through brokers, is a partnership which is secretive enough. Fund-management companies do not often need to raise money in public markets, so many have no desire for a listing. Maybe they also do not want to be at the mercy of interfering outsiders like, well, themselves.

The operation that Ms Johnson inherits has only recently completed a fairly harrowing transformation. Behind Fidelity's early success were aggressive, iconoclastic investment managers, notably her father in the 1960s and Peter Lynch in the 1970s and 1980s. Internal management, such as it was, meant crowding everybody into a single room and letting them out-shout each other. By the mid-1990s, Fidelity's growth had at last caught up with it. Performance suffered, the company became a target for criticism and key fund managers quit. Robert Pozen, Fidelity's general counsel, was the choice to manage a turnaround. He did remarkably well.

Funds which previously operated with autonomy were reorganised into small groups overseen by managers (Ms Johnson among them) and linked together through new information technology. Managers stopped leaving, and performance improved. Out of fear that he would be feeding a bubble, Mr Pozen publicly rejected the creation of an Internet fund back in 1999, when investors were pounding the table for one.

It was a bold investment call, worthy, in its way, of the best picks made by Mr Johnson or Mr Lynch. When dotcom shares collapsed, the recriminations were aimed at other firms. Ms Johnson will have much to live up to.

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Weighting share indices

Flotsam and jetsam

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From The Economist print edition

MSCI announces some long-awaited index changes

OLD-FASHIONED investors may be inclined to grumble as they assess the impact of the decision by Morgan Stanley Capital International (MSCI, a leading provider of equity indices) to overhaul the way it treats the companies it tracks. The share prices of some will rise, and others will fall, not because of any change in the companies' profitability, but thanks simply to a new weighting methodology.

MSCI has decided to weight companies in its indices according to the number of shares that are freely tradable rather than their total market capitalisation. It will also increase the share of each market that it covers, from 60% of the market's capitalisation to 85% of a free-float adjusted capitalisation, meaning that more and smaller companies will go in. Because a lot of money now simply mimics the shares held in various MSCI indices, a group of "index-tracker" fund managers will now be obliged to buy and sell the same shares at much the same time. Billions of dollars could shift between and within markets.

In MSCI's new world, the stockmarkets of Britain and America gain, largely at the expense of Japan, France and Germany, where more substantial chunks of companies tend to be held by governments, founding families or other companies. Emerging markets will be hit as well: the total value of the Emerging Markets Free Index, which represents 26 emerging markets, will fall by two-fifths, from $950 billion to $560 billion. At the sectoral level, telecommunications and technology-equipment companies will see the largest drop in weighting.

MSCI is the last big index provider to have made a shift to weighting according to free-float, after its main rivals, FTSE International, Standard & Poor's and Dow Jones. The aim is to tie a company's weight directly to the number of shares that investors can buy. Under the old system, the prices of some shares were pushed up because investors could not buy enough of them to reach the required index weight.

Calculating free-float indices is tricky. MSCI itself pointed out in a consultation paper last year that distinguishing between strategic holdings and free-floating shares is, to some extent, a matter of judgment. Trustworthy information on share ownership is often hard to find.

Levels of disclosure vary, says Giacomo Fachinotti, head of the index committee at MSCI. In the Netherlands and Greece, he points out, companies do not have to disclose share blocks until they reach 5% of issued shares. In Hong Kong the trigger point is higher, at 10%. Free-float methods therefore threaten to reward companies and countries that obscure their shareholder bases. That would be a perverse outcome, especially since MSCI hopes that its new methodology will, in time, change the way in which companies structure and disclose share ownership.

The big question for investors is how to make money out of MSCI's changes. Because the index-tracking lot have no choice in what they eventually do, traders around the world are trying to take advantage of them. Although index-huggers, with MSCI's help, are trying to be subtle—a "provisional" index allows them to spread their changes over a year—they are still vulnerable. The simplest strategy would be to jump early into the shares that passive fund managers will eventually need to buy, and then sell them at an inflated price. A chance, then, for active managers to prove their mettle.

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American share prices

A poor average

May 24th 2001
From The Economist print edition

Ignore the Dow. Most American share prices are still well below their peaks

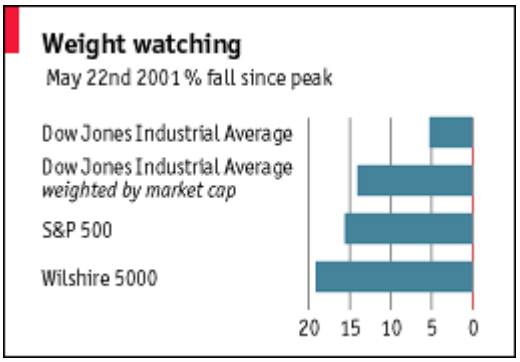
THIS week the Dow Jones Industrial Average came to within just 3.3% of its peak in January 2000. To judge by the average, the bears have retreated and equity losses have been all but restored. Was the past year just a bad dream?

Well, the Dow may be the best-known stockmarket barometer, but it is also the least reliable. It is a crude average of 30 share prices. In most other stockmarket indices, share prices are weighted by market capitalisation. When Charles Dow first published his index in 1896 there were no computers, so this crude method had advantages. He simply added up the various share prices and divided by the number of stocks. Over time the divisor has been adjusted to take account of stock splits.

A dollar increase in the share price of the biggest firm thus has the same impact on the Dow as a dollar increase in the share price of the smallest one. This is misleading, so *The Economist* has recalculated the Dow, weighting shares by their market capitalisation. On this basis, the Dow is still down by 14% from its peak. The broader market indices, such as the Wilshire 5000, are down by even more (see chart). In other words, investors' portfolios have suffered bigger losses than looking at the Dow alone would suggest.

The difference comes mainly because it is some of the larger companies that have seen the biggest falls in share prices. Microsoft's share price is still 38% below its level in January 2000. Boeing, by contrast, has gained 50%—but in January 2000 its market capitalisation was just 7% of Microsoft's.

At the stockmarket's bottom in March, investors were comforted by the fact that the Dow had fallen by less than 20%, the conventional definition of a bear market. In fact, if it were weighted, the peak-to-trough decline would have been almost 30%: easily good enough for a grizzly.



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Economics focus

The red and the black

May 24th 2001
From The Economist print edition

Only two cheers for fiscal prudence

JUST like citizens, a government ought to balance its books: so say politicians who want to appear responsible. The mantra these days is balanced budgets or, even better, budget surpluses, as in America and Britain. There are no longer many vigorous defenders of large budget deficits. Only the truly hard-pressed—an Argentina, say, or a Japan—should think of resorting to deficit spending. But hang on a second. A government's bottom line is just a number. So how much does it really matter?

A traditional argument against balancing budgets dwells on the economic cycle. As an economy grows, and employment rises, tax revenues increase. When the economy turns down, fiscal transfers and other spending might be expected to rise, even as tax revenues fall. Far better, this argument goes, if governments balance the budget over the economic cycle rather than feverishly seeking to balance the books every year.

There are more fundamental problems over the idea of balancing the budget, however. Budgeting weighs the benefits of spending against the costs of raising taxes and carrying debt. The outcomes of these three activities—spending, taxing and borrowing—follow some simple rules, on the whole. First, the more a given government spends, the less benefit accrues from the last dollar spent. That is because the most pressing needs should be funded first. Second, the more a government taxes, the more painful it is for the last dollar to be taken from a citizen; the fewer dollars you are left with, the more each matters.

And third, the more a government borrows, the greater the risk that the last dollar borrowed will damage private capital markets: it "crowds out" private (and presumably more productive) investment competing for the same dollar. The future cost of repaying the last dollar borrowed, and the chance that the dollar will tip the scales towards default, also rise with the stock of debt outstanding. For this reason, carrying $2 trillion in debt is more than twice as harmful as carrying $1 trillion.

Assuming, for now, no political constraints, then totting up these costs and benefits over, say, a couple of decades would be a good way to decide what a government's bottom line should be, and how it should be paid for. When public debt and tax-financed spending are relatively low, a deficit may be preferable. When taxes amply cover the legitimate functions of government, then a surplus can help provide against future deficits.

This model assumes that the cost of raising money increases with the scale of taxation and debt, and that the additional benefits of spending decline. Fiscal restraint is therefore a virtue. Yet, from a purely economic standpoint, it will almost never be true that a perfectly balanced budget—or, for that matter, any one, fixed target for government accounts—will be the best solution.

That has not stopped America from considering a new balanced-budget act, or the European Commission from decreeing that the budget deficits of its members must not exceed 3% of their respective GDPs. Why? Well, rules of thumb are simpler than steering by complex calculations. Rules can discipline politicians, too. Without them, governments can run up a mess of deficits that is left to successors to sort out—recall the boom-and-bust policies of America and Britain in the 1980s.

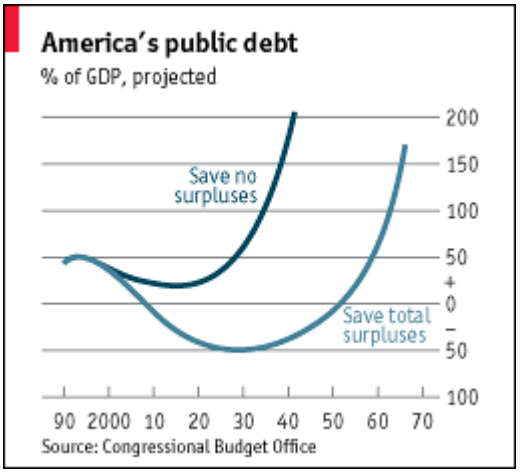
Rules also ensure that changes in fiscal policy do not happen abruptly. Smoothness is good in quiet times—though clearly not when governments face an urgent need for spending, such as in wartime or in a period when tax collection would be particularly painful, such as during a prolonged slump. Even in less extreme situations, one size is unlikely to fit all, as Europe's fiscal limits are meant to do. And well-intentioned budget rules can have another perverse outcome: they tempt politicians to fudge the numbers.

Taking the long view

Rules or no, politicians tend to act for the next election when it comes to budgeting. They try to push the burden of repaying debts far into the future. And long-term threats to fiscal health, such as the demands of an ageing population or structural impediments to the economy, can get ignored in the process.

In Japan, for instance, attempts to jump-start the economy through heavy deficit-spending have fallen flat. There is neither sufficient monetary easing nor enough structural reform to accompany the stimulus, and investment has failed to recover. America makes the problem still clearer. Given the huge predicted growth in entitlement programmes, mechanical increases in spending will, from the next decade, push the country deep into debt (see chart), if nothing is done.

Saving its surplus to pay off future debts, if that were politically and economically feasible, would keep America in the black for an extra 12 years. Washington is committed to reducing federal debt, but little enthusiasm exists for saving now against debts to be incurred in future. The time available for phasing in reforms of costly programmes such as Social Security and Medicare is thus half as long as it might otherwise be. Yet the alternative, raising taxes again and again, is hardly more attractive.



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European economies

And now, the S-word

May 24th 2001 | FRANKFURT
From The Economist print edition

Slow growth and stubborn inflation are dogging the euro area—and its currency

ANOTHER week, another lot of bad news from the euro area. At least the figures from Germany, the area's biggest economy, were largely expected. Industrial confidence slid (again) in April; feeble consumer spending, despite tax cuts, restricted GDP growth to 0.4% in the first quarter. But France, until now a bright spot, is also dimming. Growth in the first quarter, at 0.5%, was weaker than expected, and the figure for the last quarter of 2000 was revised down.

Creeping disillusion over Europe's ability to shrug off America's slowdown is weighing on the euro: this week it fell below 86 cents for the first time in six months. Another burden, though, is the euro area's inability to shrug off inflation. In none of the area's 12 countries is the "harmonised" inflation rate below 2%, the top of the range set by the European Central Bank (ECB). Already 2.9%, the euro-area average is likely to rise before it falls. Numbers from six German states point to a national inflation rate of 3.5% in May, up from 2.9% last month. Some commentators have started talking of stagflation.

Why, if growth is slowing, is inflation rising? Up to a point, says David Mackie, an economist at J.P. Morgan, this was to be expected: when economies cool, it usually takes a while for inflation to peak. Look 12-18 months ahead, and the chances are that price pressures will have eased. Most forecasters think that inflation will be below the ECB's 2% threshold by the end of the year.

The course of inflation, and interest rates, will depend partly on whether rising prices feed into wage demands. When it cut rates two weeks ago, the ECB seemed optimistic. But it is in no hurry to ease again, and will keep a close eye on rising prices of food, especially meat, which explain much of the persistence of inflation.

In Germany, for example, the retail price of pork has risen by 15-19% in the past year, depending on the cut. That reflects the BSE outbreak, which cut demand for beef, and measures against foot-and-mouth disease, which have restricted supplies. Funnily enough, beef prices have also risen, by 4%, despite a drop in demand. According to the agriculture ministry, supply also fell fast: meat disappeared from shelves, cows were culled and slaughterhouses refused to accept cattle. That has kept prices up, it seems—and maybe interest rates, too.

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Trade spats

Reprieve

May 24th 2001
From The Economist print edition

A ruling on American export subsidies is delayed again

TICK, tick—the doomsday clock for transatlantic trade has been pushed back a couple of minutes again. Last week the World Trade Organisation (WTO) decided to delay until June 22nd its interim ruling on the legality of an American export subsidy. Still, the eventual ruling is likely to find fault with America. Some urgent patching-up is needed to prevent a new trade war.

At issue is America's foreign sales corporation (FSC) tax code, which grants income-tax rebates to American exporters. Just before a deadline set late last year to comply with a first ruling against the FSC law, Congress squeezed through a slapdash replacement. The European Commission threatened to impose $4 billion a year in punitive tariffs on American exports if it failed to pass WTO muster.

Arbitration began, the matter went back to the first tribunal, and arbitration was then suspended. Every delay pushed the final decision closer to a WTO meeting in July meant to set the agenda for the Qatar ministerial summit in November. Now the decision will not become public until August 13th.

Timing counts. America wants to act as Europe's partner in launching a new trade round. Expecting an adverse ruling on the FSC case, Robert Zoellick, America's trade representative, has pleaded with the commission to delay the tariffs. He compared the $4 billion in punitive measures to a nuclear weapon. It could blow any chance of co-operation with Europe on a new round.

Yet Mr Zoellick's colleague, Don Evans, America's secretary of commerce, is sanguine. He says the FSC case is relatively small and can be resolved in time for the July talks. If he is wrong, America could appeal, delaying any retaliation until after the Qatar meeting. Even so, $4 billion is over ten times the combined tariffs imposed during the transatlantic disputes over beef and bananas, which kept tempers hot for years.

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Life insurers in Japan

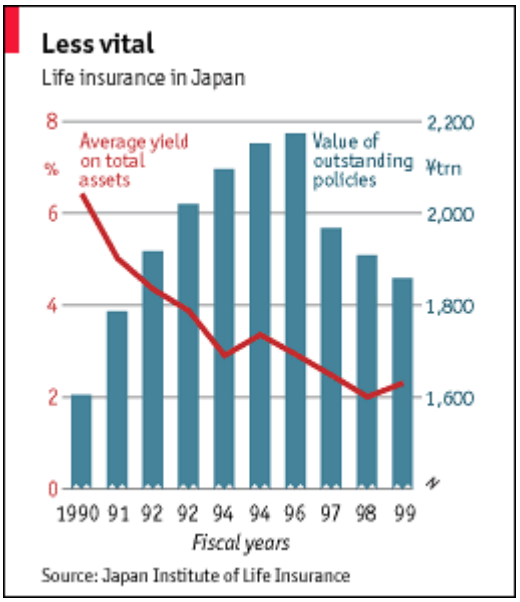
A losing roll

May 24th 2001 | TOKYO
From The Economist print edition

Japan's life-insurance industry is hobbled by poor returns

FOR almost a decade, Japan's life insurers have been losing money. Five have collapsed in the past year. Nobody expects the rest to announce anything other than awful annual results on June 4th.

Their problem is years of low interest rates in Japan, which have led to falling annual returns (see chart). This means that life insurers are unable to match the high pay-out rates they have guaranteed on existing policies by investing the premiums that are paid in. In the year to March 31st, the ten biggest insurers are expected to have lost ¥1.4 trillion ($12.7 billion) from this mismatch alone. Then there were dud investments in equities and property, and also bad loans to other sickly companies.



To be fair, the fault is not wholly the life insurers'. One reason they set unrealistically high pay-out rates in the 1980s was that the government's own life-insurance business, run by the post office, could compete in the knowledge that its losses would be plugged with public money.

For the past few months a government panel has debated whether to help the industry out by allowing them to lower their annual pay-out rates. Under current law, insurers are not allowed to do this unless they have gone bust. Proponents of the scheme argue that policyholders would rather see returns shaved a bit now than have them cut drastically once insurers collapse. Two options are under discussion. One is to issue a government directive that forces all life insurers to cut their pay-outs; the other is to revise laws to allow individual insurers to cut rates.

The first option is the least plausible. Not least, instructing the industry to shift the burden of losses on to policyholders would lead to all sorts of legal headaches for the government. The scheme has also met fierce opposition from Nippon Life, the country's biggest life insurer, which can afford to tough things out longer than its rivals. Some panel members are also concerned that the move could lead disgruntled consumers to turn their back on the insurers altogether, worsening their plight. So the panel is leaning towards letting weak companies cut their guaranteed rates of return, so long as they get approval from a majority of policyholders, sack their managers and submit a detailed restructuring plan.

There are several things wrong with this idea, the critics say. One is that it does nothing to tackle the industry's opacity. Since most life insurers are not listed companies but mutual societies, disclosure standards are poor. It is hard to work out quite how bad companies really are. For example, figures showing the mismatch between guaranteed pay-outs and investment returns are not published. Instead, life insurers produce complicated numbers that show their "negative yield"; even they admit that this does not represent the true value of the mismatch.

The ambiguity has caused confusion. Most life insurers have pleaded weakness when pressing to be allowed to break contracts and lower pay-out rates. The same insurers have also argued that they make gains from lower-than-expected mortality and expense rates, which, they say, more than cover losses from annual pay-outs. That raises the question why insurers need rescuing at all.

Another problem is that few insurers are likely to use the scheme. Since Toho Mutual, a medium-sized insurer, collapsed in 1999, consumers have become nervous about the safety of their policies. Life insurers are now worried that the slightest whiff of trouble will lead to floods of cancellations, as it did at

Chiyoda Life and Kyoei Life before they collapsed last year.

There seems, in short, little the government can do. Not even reigniting inflation would work. Higher long-term interest rates would lower liabilities, because they would reduce the gap between pay-out rates and investment returns. But they would also harm the asset side of insurers' balance sheets, as bond prices fell.

Where the government could help to improve the industry's credibility is by tightening disclosure rules. So far, its well-meant discussions have merely illuminated the extent of the industry's problems. Still, for every loser there is a winner. Big foreign companies such as America's AIG and Canada's Manulife have been snapping up failed insurers. Consumers' lost faith in Japanese insurers may be restored by foreign ones.

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Share valuation in Asia

Throw out the rule-book

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From The Economist print edition

Share-price multiples that may work in the West do less well in Asia

THE developing markets of East Asia have got the better of many a western fund manager over the years. Usually, it suits the unlucky investor to blame his underperformance on Asia's crony capitalists, its weak rule of law or its inefficient capital markets. Perhaps, however, the fault lies in assuming that the various multiples, dividend-discount models and other fancy metrics that they use to value shares in America or Europe should automatically work in Asia as well.

EPA

Three think the price is relevant

Markus Rosgen, a Hong Kong-based analyst at ING Barings, a European bank, has long suspected as much. He crunched numbers to test the relevance of a wide range of valuation tools in various East Asian markets. The results are surprising.

The biggest shocker, especially to "value investors" of the Warren Buffett school, is that the share price—a rather crucial number, you might think—has historically been almost wholly irrelevant for making good investment decisions in Asia. Rather, the winning strategy has been to buy shares in those companies that achieved the highest returns on equity in the previous accounting period, irrespective of their current market value.

Mr Rosgen is puzzled, but suspects that the dismal record of Asia's profit forecasters is to blame. So unreliable have their hunches been that last year's numbers are still the least bad metric. Discounting cashflows, in other words, is usually a waste of time in Asia: the cashflow projections will be wild guesses, as will the discount rate to be applied to them. Multiples such as the ratio of "enterprise value" over "EBITDA" (earnings before interest, tax, depreciation and amortisation) are also "pretty much useless."

Local idiosyncrasies count. In South Korea, whichever companies did worst in the previous six months have tended to do best in the next year. The government has never quite kicked its habit of bailing out corporate dogs. In effect, says Mr Rosgen, this is like an "implied put option" on South Korea's worst companies.

In China and the Philippines, by contrast, the best strategy has been to concentrate on companies' debts. This means disregarding not only the share price, but also the income statement. Instead the focus should be on the ratio of current assets to current liabilities on the balance sheet. On the high-tech island of Taiwan, however, looking for the highest ratio of research and development to sales has produced the best portfolio returns.

If all this sounds a bit scary, investors can still find some crumbs of comfort. Mr Rosgen also discovered that Asian companies, unlike western ones, are old-fashioned in at least one way: they pay dividends. In Singapore, Hong Kong, China and Malaysia, well over half of all companies produce dividend yields that are higher than interest rates on bank deposits. In America only 7% of companies do that. Indeed, two-thirds of the investment returns to be had in Asia since 1991 have come not from capital gains but from dividends. High dividends are often seen in corporate-finance theory as a wasteful use of scarce capital. They are appreciated by investors in Asia, even so.

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The World Health Organisation

A triumph of experience over hope

May 24th 2001 | GENEVA
From The Economist print edition

Three years ago, the World Health Organisation changed command. Has the new captain kept her promises?

Get article background

SMOOTH sailing is generally the rule on Lake Geneva, but at least one of the United Nations agencies on its shores has run into choppy water. On May 22nd, the World Health Organisation (WHO) concluded its annual jamboree—the World Health Assembly—which brings together representatives from the organisation's 191 member states to take stock of what has been achieved and to look forward to what should be done.

For more than a week, these delegates have scaled mountains of material on topics ranging from infant feeding to depleted uranium. But although the devil is in such details, the big picture matters, too. When the present director-general, Gro Harlem Brundtland, took over three years ago, the sweeping of new brooms was promised. Her predecessor, Hiroshi Nakajima, was widely seen as a disaster. His management style, cynics suspected, was modelled on that practised by the Japanese government—in other words a combination of weak central control and financial incompetence.

Unlike Dr Nakajima, Dr Brundtland has had some experience in government. She was prime minister of Norway on three occasions. That was seen as being in her favour, but now some people are having second thoughts. In an organisation as protean as the WHO, her executive instincts may have gone too far. She is running the organisation, as one observer put it, as if she were still a prime minister—insulated by a close-knit cabinet of advisers who try to muzzle internal dissent in order to stick to a strong party line.

Heal thyself

That is a view echoed by several member states. Brazil and South Africa, for example, have expressed frustration at what they see as initiatives issued by the WHO's top brass without discussion with the countries supposed to implement them. Since the organisation's constitution says that its mandate comes from the bottom up, not the other way round, they have a point. But things had clearly got out of control under Dr Nakajima, and discipline needed to be imposed.

Dr Brundtland has certainly tried to do that. She has shaken up the organisation's headquarters and put more than half the staff on short-term contracts. According to Kelley Lee of the London School of Hygiene and Tropical Medicine, a long-time observer of the WHO, this reform has been successful at reining in the powerful and largely independent units that once flourished within the headquarters. It has not, however, dealt with the deeper problem of the six regional offices that are supposed to translate WHO policy into local action, but which have often followed courses at odds with the centre's.

The initiatives that have been pouring out of Geneva have also come in for criticism. They include high-profile campaigns on malaria and tuberculosis (TB), which, on the face of things, seem worthy enough. Some people close to the organisation argue, however, that they are just old wine in new bottles, and that apart from their snappy slogans, such as "Rollback Malaria" and "Stop TB", they have little to show for themselves. It is a charge that Dr Brundtland vigorously denies. She points, for example, to declines in the incidence of malaria in countries such as Turkey since Rollback Malaria was launched in 1998.

For the time being, her strategy is paying off, not least in financial terms. Big donors such as America and Britain are positive about the changes, and “extrabudgetary” funding (the money that countries contribute for special projects) has increased by 40% since 1999—even though America is about to cut its share of the WHO’s official budget from 25% to 22%, in line with its reduced contributions to the United Nations as a whole.

Malaria and tuberculosis have always fallen within the WHO’s purview. But Dr Brundtland’s campaign against tobacco is genuinely novel. This new direction brings new critics, and also accusations that the organisation is exceeding its remit. Tobacco companies have lambasted the WHO’s attempts to curb smoking through the creation of an “international framework convention on tobacco control”. This would set out principles and protocols to help countries tackle such issues as cigarette smuggling and advertising.

On the other hand, some non-governmental organisations, such as Health Action International in the Netherlands, worry about the opposite phenomenon: cosying up to industry, rather than bashing it. They fret, in particular, about potential conflicts of interest arising from the WHO’s overtures to drug companies. (These are intended to encourage the companies to lower their prices and improve access for people in the world’s poorest countries, and have borne fruit in deals such as that just signed with Novartis to supply a new malaria treatment at cost.)

On top of that, Dr Brundtland took a pasting last year from some of her own experts, and from some WHO member states, over an attempt to rank the world’s health-care systems. These people felt that the exercise, which led to such curiosities as Morocco outperforming Australia, was deeply flawed, and that their criticisms had fallen on deaf ears. Since then, further remonstration has led to this year’s league table being shelved.

While such intransigence sometimes rankles, it does make Dr Brundtland a passionate public advocate. Under Dr Nakajima, the WHO spoke softly. Today, the director-general is never far from the podium, preaching the gospel of investing in health care as the key to eradicating poverty, as well as being good in its own right.

As Richard Feachem, the head of the Institute for Global Health, part of the University of California, points out, over the past three years Dr Brundtland has moved health, and the WHO, off the sidelines and into the centre of the global debate on development. AIDS, malaria and tuberculosis are now the stuff of G8 summits, special sessions at the United Nations and, if Kofi Annan, the UN’s director-general, has his way, of a $10 billion global health fund. Dr Brundtland sees such advocacy as a natural extension of the WHO’s traditional roles, complementing rather than detracting from its original objectives of setting health-care standards and exterminating such dread diseases as smallpox and polio.

The WHO is a complex organisation working in an increasingly politicised environment. It is no longer the only global body involved in public health, nor is it the best endowed; the World Bank and the Gates Foundation have pretty deep pockets, and are muscling in on its territory. Nevertheless, though many people find Dr Brundtland’s brusque bedside manner hard to take, few deny that her patient is in better condition than before she came. How long, and what shape, a full recovery will take is, like most prognoses, a matter of waiting and seeing.

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Discovering what genes do

Shooting the messenger

May 24th 2001
From The Economist print edition

A new way to detect the jobs done by individual genes works in mammals

JUST occasionally, nature gives you something for nothing. In 1968 Hamilton Smith and his colleagues at Johns Hopkins University, in Baltimore, found that certain bacteria produce molecules called restriction enzymes. These cut strands of DNA in particular, predictable places. That led to a lot of useful technology, the most familiar, perhaps, being the genetic “fingerprints” used to identify criminals from DNA left at the scenes of their crimes.

Bacteria do not make restriction enzymes out of the goodness of their hearts, nor to help catch criminals, of course. The enzymes are there to do a job, in this case chopping up the DNA of invading viruses. Over the past couple of years, researchers have begun to make use of a second anti-viral mechanism, known as RNA interference (RNAi), that may have even more value than restriction enzymes.

RNAi blocks the actions of individual genes. That means that a gene’s function can be worked out from the consequences of the blockage. The technique could even lead to a new class of drugs that work by suppressing the activities of individual genes. Unfortunately, until recently, RNAi could not be made to work in adult mammals (including people)—or, rather, it worked too well. Instead of blocking the activities of individual genes, it shut down the whole cell, killing it. But a paper just published in *Nature* by Thomas Tuschl and his colleagues at the Max Planck Institute for Biophysical Chemistry in Göttingen, Germany, seems to have overcome that little difficulty.

RNA is the messenger molecule that transfers genetic information from a cell’s nucleus (where genes are found) to its cytoplasm (where the everyday business of staying alive is carried on). Individual RNA molecules are edited copies of the nuclear genes, and RNAi stops them delivering their messages.

It was a mere two years ago that somebody worked out why this happens. Andrew Fire of the Carnegie Institution and Craig Mello of the University of Massachusetts found that it was due to a cell’s response to double-stranded RNA. Normal messenger RNA is single-stranded; in nature, only viruses produce a double-stranded version of the molecule. It therefore makes sense for a cell to respond to double-stranded RNA by destroying any RNA lying around that resembles it, on the assumption that this, too, is viral. So researchers simply have to make artificial, double-stranded RNA that matches a gene they wish to investigate, and introduce it into a cell. The appropriate messengers will then be efficiently mugged and the gene in question silenced.

The way a cell does this is still a mystery. But that has not stopped people making use of the technique. *C. elegans*, a tiny threadworm beloved of geneticists, has been positively pummelled with such double-stranded ambuscades. Around 5,000 of its 19,000 genes have been interfered with in this way by researchers working in Germany, Britain and America, and much useful information about how the worm develops from a fertilised egg into an adult has been found. That is important, because the human genome project has shown that worms and people are sufficiently similar at a genetic level for meaningful inferences to be drawn about the latter from the former. It would, nevertheless, be nice to be able to do the same experiments in mammals.

Thanks to Dr Tuschl’s work, that should now be possible. In worms, RNAi is carried out using long pieces of double-stranded RNA. Dr Tuschl and his colleagues have found that it is the length of these molecules that stops the technique working in mammals. However, short strands—which can still carry enough genetic information to identify a gene unambiguously—do work in mammalian cells. They inhibit only the target gene, not the whole cell. Why that should be is not yet clear. What is clear is that in this, as in so many things, less is more. Expect to read a lot more about RNAi in future.

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Salmon conservation

Something fishy

May 24th 2001
From The Economist print edition

There are more salmon in the Columbia River. Not everybody is happy

THIS spring, around 375,000 adult chinook salmon are expected to make their way over the Bonneville hydroelectric dam as they swim up the Columbia River between Washington state and Oregon to reach their spawning grounds. In one day alone, 27,000 chinook leapt and bounded up the salmon ladders next to the dam—almost three times the number recorded in the whole of 1995. For many, this is a welcome display of the sea's bounty; for the first time since 1977 there are enough chinook in the river to allow them to be fished commercially.

Sadly, though, the news is not all good, for some 80-90% of this spring's chinook are not wild fish. Instead, they were raised from eggs in artificial hatcheries and released into the river several years ago—whence they swam to the ocean along with their wild cousins, to feed, grow and, if they survived, to return to the river to spawn. Salmon learn where to spawn from the smell of the water in which they grew up. This means that hatchery fish tend to return to their natal hatcheries. Over the years, therefore, each hatchery's population has become genetically distinct, both from that of other hatcheries, and from the various wild populations.

They are not only distinct, but they also seem to be affecting the population of wild salmon. A paper published in the *Proceedings of the Royal Society B,* by Phillip Levin and his colleagues at America's National Marine Fisheries Service, explains this. The researchers looked at the survival of wild chinook in the ocean over a period of 25 years. What they found was that as hatchery fish are released in larger numbers, wild fish have become less successful, particularly in years when ocean productivity is low. Probably, this is the result of so-called density-dependent selection—a fancy way of saying that in years of poor productivity, the hatcheries add so many hungry salmon mouths that there is not enough food to go around. It might, though, mean that the cossetting that hatchery-bred salmon receive during their first year of life gives them a head start when times are tough.

Whatever the reason, the wild chinook is a threatened species, and so, according to the Endangered Species Act, something has to be done to protect it. Since hatchery fish are genetically distinct from the wild ones, they are not, in the eyes of the law, a sufficient substitute.

The arguments, though, are not only about the genetic differences between different groups of fish. Jim Lichatowich is the former assistant chief of fisheries for Oregon, and now an independent consultant. He says that over the past 125 years hatchery fish have been released in the search for a simple solution to the problem of excessive demand on water resources and the damage it has done to fish stocks. But because monitoring and evaluation has been so poor, Oregon's Department of Fisheries and Wildlife—which runs some hatchery programmes—has no real idea whether the number of adult fish produced by those programmes is worthwhile. They are certainly not delivering the tens of millions of salmon that they were meant to. The only reason they continue at such a pace, argues Mr Lichatowich, is that they are the main source of funds for the agencies that operate them.

The dramatic numbers of chinook that returned this year have less to do with a wise investment of taxpayers' money than with unusually favourable sea conditions. Changes in Pacific wind patterns and temperatures have caused an upwelling of nutrients from the bottom of the ocean off the coast of Washington and Oregon. Things have not been this good for 20 years. Unfortunately, nobody knows when it might happen again, nor how to predict such conditions. Even if they did, no amount of intervention by the Department of Fisheries and Wildlife could bring them about.

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Car safety

Electronic angels

May 24th 2001 | DETROIT
From The Economist print edition

A new chip should stop children dying of heatstroke

NOT content that their products should be safe merely when they are being driven, car makers plan to add safety features that operate when they are stationary. The first of these, an anti-heatstroke chip, was unveiled by General Motors earlier this month.

Cars, with their large glass windows, act as greenhouses. On a summer's day the temperature inside can reach 70°C. As a result, scores of children and hundreds of pets die each year from vehicle-related heatstroke.

The company's chip, which is embedded in a vehicle's roof, uses a low-power radar to detect movement inside the passenger compartment. It is, GM claims, sensitive enough to notice the breathing of a newborn baby. The chip also monitors the temperature of the vehicle's interior. If that becomes dangerously high while the vehicle is occupied, the chip reacts by sounding the horn.

That, GM hopes, will be enough to attract the attention of a passer-by—who would, presumably, find the driver, alert the authorities or, if all else failed, break in and rescue the child (or pet). An alternative might be to link the sensor to the OnStar "telematics" system with which GM is connecting its latest vehicles electronically to the outside world. Using OnStar, the chip would telephone the wayward parent or even the emergency services, without having to rely on the kindness of strangers.

The heatstroke sensor could turn out to be the first of a series of electronic guardian angels. Another device that GM is testing measures levels of carbon monoxide in the passenger compartment, in case the exhaust is leaking. The firm's researchers are also developing sensors that monitor eye and head movements, looking for signs that a driver is drunk, or is falling asleep at the wheel. Ford, too, is working on chip-based nannies. It reacted to the GM announcement by announcing a heatstroke sensor of its own. This one, apparently, comes with a bonus for the paranoid. It can also warn a driver if somebody has broken into the vehicle and is hiding inside it.

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Russian history

Not as old as it looks

May 24th 2001
From The Economist print edition

A sweeping new history of Russia finds breaks as well as continuities in its past

Russia and the Russians
By Geoffrey Hosking

Harvard University Press; 718 pages; $35. Allen Lane, The Penguin Press; £25

Buy it at
Amazon.com
Amazon.co.uk

THERE used to be two kinds of Kremlinologist. One saw an almost unbroken continuity between Bolshevik rule and previous forms of Russian statehood. The other took virtually at face value the communist claim to have made an irreversible break with the tsars, indeed with history.

During its seven decades of existence, the Soviet state's own theorists themselves wavered on this question. In the early days of post-revolutionary zeal, some Bolsheviks genuinely believed that they were creating a new political formation that would transcend boundaries of geography and culture, and belong in equal measure to the workers of the world.

Less than 25 years later, at the height of the second world war when the survival of Russia itself was in peril, Josef Stalin reverted dramatically to memories of the tsarist past. His wartime leadership astonished its western allies by ordering up huge quantities of gold braid and shoulder straps to adorn officers' uniforms. Stalin also instituted military decorations named after Mikhail Kutuzov and Alexander Nevsky, the defenders of the nation against the forces, respectively, of Napoleon and the medieval Teutonic knights.

In the post-war years, a school of communist scholars known as national Bolsheviks earnestly compared the achievements of Stalin with those of the tsars, in party journals with large runs but small readerships, while a rival school, in the same journals, continued to propound the ideals of proletarian internationalism. These differences are of more than antiquarian interest. Their traces are visible today in the newest repository of east Slavic statehood, the semi-democratic Russian Federation, which is as confused as ever about its cultural and historical legacy.

In this comprehensive and intelligent survey of Russian history for the general reader, Geoffrey Hosking gives us the grand sweep. As he follows the twists and turns of Slavic history from the principalities of Kievan Rus in the late ninth century to the presidency of Boris Yeltsin, he holds back from putting forward a single, all-purpose theory of culture or geography to explain Russia's idiosyncrasies. But certain strong themes emerge.

One task facing any would-be ruler of the north Eurasian mass is to establish a coherent administration in such a huge, featureless landscape which is easy to invade but hard to occupy. A second difficulty is shared by any tradition-bound, authoritarian state facing competition from suppler societies. The strengths needed for success—economic prowess, intellectual vitality, thriving cities—are things likely to undermine old hierarchies and values. A third problem is imperial over-stretch. Russian history has shown—not just in 1991—that, when defending distant borders proves too much, the Russian state can

contract as dramatically as it can expand.

While alive to these continuities, Mr Hosking writes most originally about the breaks with the past. As 150-year-old nationalist myths continue to wear down the Balkans, he provides a firm and welcome reminder that an ethnically defined Russia was a relatively recent and deliberate creation, influenced by state-building elsewhere in Europe.

Only in the 19th and 20th centuries did Russia's rulers attempt, in different ways, to reconcile the multi-ethnic character of their dominions with a Russification, first of the empire's elites and then of the people as a whole. Perhaps because this project failed, the state now ruled from the Kremlin is smaller and more homogenous than either the Soviet Union or the territory of the tsars. But as Mr Hosking argues in his final pages, questions remain about the *raison d'être* of the Russian nation, and hence of the Russian state.

Is Russia, he asks, the "creator and sustainer" of a multinational empire? Will it be the core of an "eastern-Slavic union" which includes Ukraine and Belarus? Even without them, the national question is still there. Is the Russian Federation to be a standard-bearer for ethnic Russians or Russian-speakers (not the same) beyond its borders? And, if so, where does that leave citizens of the Russian Federation who are not ethnically Russian?

Prudently, Mr Hosking leaves these issues open, ending instead with the cautious observation that, though Russia is one of history's great survivors, it will need "statesmen of unusual ability and vision" if it is to last out the 21st century.

One looming challenge is demography. Can Russia's declining population retain control of northern Eurasia in the face of a fast-growing China? With a population so tiny for its size, Russia faces a military choice. It can try to organise its defences on western lines, paying for armed forces from an essentially civilian economy. Or it can remain a semi-mobilised society whose schools and enterprises, in many ways, serve military needs.

A second challenge is common ideals. Beliefs matter in geopolitics as much as guns. Communism, which turned industry and secularism into a kind of religion, complete with clergy, was Russia's way of being modern. How will Russia be postmodern? Russian cities often seem to have the worst of the new and the old: families are if anything weaker than in the West, while the safety net of social-welfare does not exist either. An optimist would argue that at least such atomisation makes it harder to imagine the return to a totalitarian ideology such as communism or fascism. Perhaps so. But Russians will need some stronger reason for holding their state together. In the past, as Mr Hosking's excellent historical survey reminds us, one of the most dependable sources of Russian legitimacy was defence against foreign enemies. Will Chechens be enough?

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Popular classics

Ich bin ein Cowboy

May 24th 2001 | RADEBEUL
From The Economist print edition

Modern Germany's favourite author will come as a surprise

WHEN American GIs poured into Germany in 1945, they were astonished to discover that German children, after 12 years of Nazi rule, could be found decked-out in buckskins and feathers and playing "Indians". Every spring in Radebeul, a quiet Dresden suburb, tens of thousands of grown-ups do the same. The explanation for both these phenomena is Karl May (1842-1912), a Saxon weaver's son, jailbird, self-described linguist—and the man who single-handedly invented the wild west for generations of Europeans. Long before the Lone Ranger, May was giving unruly cowboys what-for, befriending Winnetou, a great Apache warrior, and generally bringing peace and order to the frontier.

Though he is virtually unknown to the English-speaking world, May is possibly the most-read German author of all time: his books have sold an estimated 100m copies to date. The Germans have a saying: "We know Goethe, but we read Karl May". Albert Einstein spent his entire adolescence under May's spell; Hermann Hesse, who called May's work "fiction as wish-fulfilment", was a life-long fan. In Germany today, Winnetou is synonymous with "Indian", and hundreds of "Indianer" clubs meet at weekends to practice tribal ceremonies in traditional costume.

No matter that May wrote his most famous "travelogues" (there were close to 80 in all) without ever leaving Saxony. Born into poverty in the small village of Hohenstein-Ernstthal, he spent much of his early adulthood engaged in petty fraud and impersonation—good training for his subsequent writing career. May's extended sojourns in jail, meanwhile, gave the voracious reader plenty of time to absorb just about everything he could get his hands on concerning strange peoples in faraway lands.

Having found his calling, the young masquerader churned out a number of first-person accounts of Arabian adventures, with considerable success. But it was the 2,000-page "Winnetou" series, completed in 1893, that turned May into a rootin'-tootin', sure-shootin' sensation. Picking up where Buffalo Bill Cody's 1889 German tour left off, he came up with the ingenious idea of presenting a western adventure in which a German novice, Old Shatterhand, out-lassos, out-hunts, out-shoots and finally out-wits Yankees and Indians alike. Throw in the hero's great alliance with Winnetou, the stoical "red gentleman", and May had created both a patriotic epic and a popular monument to the Native American race.

With the smell of success in his nostrils, May was unstoppable. He put it about that his narrator-hero's exploits were actually his own, even showing off a lock of hair taken from his "blood brother" Winnetou. He posed for photographs with "Silver Nail" and "Bear Killer", the rifles he said he and the Apache had used in the west. At his Villa Shatterhand in Radebeul, he surrounded himself with big game skins, Indian scalps, peace pipes, carpets, Arabian tea sets and other exotica. He set himself up on the German lecture circuit as the learned Herr Doktor May.

For a time even May's publisher was taken in—some scholars have suggested that May himself was too. By the turn of the century, however, these role-playing antics had begun to take their toll, and the author spent much of the last decade of his life squabbling over publication rights and narrowly avoiding scandal. In 1908, the beleaguered May finally travelled to America. But he was destined to remain a true greenhorn: he made it no farther west than Buffalo, New York.

Karl May's version of the American west bears little relation to any historical reality—which no doubt accounts for much of its charm. It remains irresistible to readers from all walks of life. Although Klaus Mann, Thomas's son and an author in his own right, accused May of being a mentor for the Führer (Hitler reread May after seizing power in 1933), movie adaptations shot in Yugoslavia in the 1960s and starring a Frenchman, Pierre Brice, as Winnetou, created a huge new following in West Germany. For its part, the East German government rehabilitated the formerly "chauvinist" author in the early 1980s and reopened the Villa Shatterhand to May fans from all over the Eastern block. May's most famous books have now been translated into more than 30 languages (fewer, admittedly, than the 1,200 the author himself claimed to have mastered). There is a museum devoted to May and his Indians in Lithuania. Not long

ago, a Nicaraguan revolutionary, Tomas Borge, claimed that May's western stories had inspired him in his political struggles.

So deeply rooted is the Karl May legacy today that the Native American Association of Germany, a small group started by Native American soldiers stationed in Europe during the cold war, has recently launched a campaign to re-educate Germans in the facts of Native American history. But they have an uphill battle against Old Shatterhand and Winnetou, who, like the west itself, were legends almost before they appeared in print. As a seasoned frontiersman tells the newly arrived Shatterhand at the beginning of one of his Great Plains adventures, "It's amazing what they make you people learn over there."

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Philosophy of knowledge

Hooking up to the world

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From The Economist print edition

NEWNESS in philosophy is rare. But this important book offers a boldly original view of the nature of knowledge. It would be disingenuous to suggest that "Knowledge and its Limits" can be fully appreciated without a substantial background in philosophy. But it would not be fair either to leave it to specialists.

Knowledge and its Limits
By Timothy Williamson

Oxford University Press; 352 pages; $35 and £25

Buy it at
Amazon.com
Amazon.co.uk

Some philosophy books present big pictures, full of compelling images and polemics, but can be loose, vague and rather short on detailed argument. Others offer rigorous arguments on detailed matters, but can seem excessively technical and pedantic, of interest only to a few scholars in a sub-discipline. Timothy Williamson's book has both merits and neither fault. A daring new picture of knowledge is skilfully supported with an argumentative verve that its author, the new professor of logic at Oxford University, has made himself known for.

To grasp Mr Williamson's originality, consider how Anglo-American philosophers have tended to set about defining knowledge. We all recognise a distinction between believing something and knowing it: there are plenty of false beliefs—many held with stubborn conviction—but there is no false knowledge, for knowing something entails that it is true. Yet there has to be more to knowledge than true belief, since otherwise we could stumble on knowledge by dumb luck: how we reach our beliefs must matter, surely, to their reliability. (Think of the difference between knowing and guessing the right answer to a multiple-choice question.) The missing extra has usually been taken to be warrant or justification, and for half a century or so argument has focused on whether "true, justified belief" provides an adequate analysis of knowledge.

Mr Williamson rejects this entire way of thinking. He treats knowledge as a mental state of its own special kind and not one that can be analysed or broken down into components. Each point is striking.

There is a philosophical view of the mind and its contents, known as externalism, that has become widely influential in recent years. Mr Williamson shares this view, but pushes it further. The rough idea is that, because many mental states crucially depend on our environment—they reach out, as it were, and hook on to the world—minds cannot be thought of as confined to our brains. Conventional externalists put beliefs into the category of mental states of this kind that are not so to speak in the body. Mr Williamson goes a step beyond to say the same of knowledge.

It is unusual, too, to take the notion of knowledge for granted as a starting point, and then treat belief as being a form of botched or would-be knowledge. Mr Williamson accepts that knowledge entails true belief, yet rejects the traditional next step of insisting—the difference is tricky but important—that it be analysed into true belief plus something else. An analogy: being red entails being coloured; but it does not follow from this that being red can be analysed into being coloured plus something else.

Other long-standing assumptions about knowledge are rebutted as the book progresses: Mr Williamson argues that knowledge cannot be defined in terms of evidence, but rather that your evidence simply is your knowledge; that we have no guarantee that we know when we are in a certain mental state; and much more besides. Throughout, Mr Williamson is bold, ingenious and original; the tradition he opposes appears by contrast stale, scholastic and uninspired. As will be expected, many parts of the book are technical and not for the faint-hearted. Yet anyone with a serious interest in philosophy will have much to learn from this challenging book.

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New fiction

Threadbare

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From The Economist print edition

RICHARD RUSSO'S sweeping prologue to "Empire Falls" is so good that readers are likely to flip through the rest of the novel wondering what went wrong. Disappointingly, Mr Russo returns to the same lunch-counter banter in the same knock-off of Gloversville, the run-down town in upstate New York where he was raised, that fills out three of his four previous novels. As ever, flawed but endearingly eccentric regular folks quaff weak coffee and wonder if the mill's gonna sell.

Empire Falls
By Richard Russo

Knopf; 490 pages; $25.95.
Chatto & Windus; £10.99

Buy it at
Amazon.com
Amazon.co.uk

Such slices of small-town life ring true enough. But repetition has taken a toll. The characters in "Empire Falls" have the pale, flannelled quality of oft-washed cotton. A fourth visit to a dwindling post-industrial New England community—full of youngsters who vow they'll get out, dreamers who wish they had and pragmatists who understand there's no place like home—cannot recreate the sense of fresh discovery found in "Mohawk" or "The Risk Pool".

The background to the story has a certain grandeur about it. The wealthy Whiting family owns half of Empire Falls, including the textile and paper mills that once made it a lively town. "Forty years ago Empire Avenue was bustling with people and cars and commerce, whereas now, of course, you could strafe it with automatic weapons and not harm a soul." Successive father figures have been chronically henpecked ("it was the particular curse of the Whiting men that their wives remained loyal to them out of spite"). Now only the icy, imperious Francine Whiting remains. Her husband has shot himself, as an alternative to shooting her. Sparing her crippled daughter anything so warm as pity, Mrs Whiting runs the townspeople's lives from her pretentious hacienda, and rarely for the better.

Enter middle-aged Miles Roby, a nice guy who might have made something of himself but was lured from college back to Empire Falls to nurse his dying mother, then enticed to stay and run the struggling Empire Grill by its owner, Mrs Whiting. It will take hundreds of pages and a heavy-handed *deus ex machina* to get Miles to do anything but muse behind his counter about starting a more interesting life elsewhere.

This is a frustrating novel. Discrete panoramic passages, occasional masterly lines, moments of deft wit are reminders of just what Mr Russo can do—Edith Wharton leavened with a touch of David Lodge. Yet he falls back on a comfortable life-going-by formula and remains shy of the scope and scale that typifies truly memorable fiction.

"Empire Falls" is streets ahead of "Straight Man", Mr Russo's last novel, but it trails far behind his best work. If Miles Roby is in a rut, so is Mr Russo. Perhaps in time he will clamber out to write a whole novel with the range and spellbinding allure of those first 16 pages.

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Literary criticism

Spinal columns

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THE true critic, observed Vladimir Nabokov, reads not with his brain but with his backbone. He waits for the “tell-tale tingle down the spine” which alerts him to good writing. Here are two collections of literary journalism written by men who trust their backbones, and to whom “maybe”, “might” and “perhaps” are the throat-clearings of less assured intellects. Martin Amis and Christopher Hitchens are both renowned stylists, and they are as capable of talking up a book as they are of tearing one down. It is a pleasure to watch them do either.

What makes Mr Amis really angry is cliché. Cliché, he holds, is not just fossilised language, it is any sort of stock response— emotional, political or literary. It is, in short, thoughtlessness, and the avoidance of cliché is therefore not just a requirement for a stylist, but a duty for the moralist. In Mr Amis’s opinion the unexamined word is not worth writing, and this is the creed by which he lambasts author after author for their “automatic” use of language. Iris Murdoch, John Fowles, D.M. Thomas, Angus Wilson, and Fay Weldon are all here brought to book in entertaining and convincing fashion. By contrast, J.G. Ballard, Don DeLillo, Shiva Naipaul and others are praised for their “qualities of freshness, energy and reverberation of voice”.

The War Against ClichÃ©: Essays and Reviews 1971–2000
By Martin Amis

Jonathan Cape; 528 pages; £20.

Buy it at
Amazon.co.uk

Unacknowledged Legislation: Writers in the Public Sphere
By Christopher Hitchens

Verso; 382 pages; $25 and £17

Buy it at
Amazon.com
Amazon.co.uk

Mr Amis’s allergy to boring and ill-considered prose affects his own writing—it brings him out in a rash of unexpected adjectives. He notices the “virtuoso triviality” of Andy Warhol’s diaries, for instance, or the “tundra-like humourlessness” of a literary scholar, or the “phosphorescent prosperity” of England in the 1980s (you need not necessarily accept the implied political sentiment to hear how neatly that last phrase suggests burn-out and showiness). These essays glitter with elegant put-downs of this kind, and you read them admiring the way in which Mr Amis keeps to his own rules about writing.

Christopher Hitchens’s book takes its title from Shelley’s idealistic proposition that “Poets are the unacknowledged legislators of the world”. Writers are not generally rulers, but for Mr Hitchens this is precisely why their engagement with politics is so significant: they stand outside it. It is common these days either to decry politically engaged literature as being aesthetically compromised, or to deny that literature has any purpose other than entertainment. But Mr Hitchens will have none of this. Literature, he asserts, can change the world, and he cites the fall of the Soviet block, “which collapsed amid laughter and ignominy, without the loss of a single life, as a consequence of a civil opposition led by satirical playwrights, ironic essayists and subversive poets.”

Like George Orwell, to whom several of the essays are devoted, Mr Hitchens’s ambition is to “make political writing into an art form”. Most of the pieces here, notably those on Rudyard Kipling, Northern Ireland, Oscar Wilde, and Salman Rushdie, achieve that. Although he is keen to bring out “the latent political intelligence of literature”, Mr Hitchens is rightly not prepared to have authors like T.S. Eliot and Philip Larkin read only through the optic of their politics; in his opinion this grossly distorts their art.

Mr Amis and Mr Hitchens have many friends, enemies and attitudes in common. Both admire Saul Bellow, Philip Larkin, Gore Vidal, Oscar Wilde and Salman Rushdie. Both write almost entirely about men. Both are appalled by anti-elitism, political correctness and cultural democratisation. And both like nothing more than a good fight. The great difference between them is this: Mr Amis, following Nabokov, thinks that “the sole end of art is aesthetic bliss”, while Mr Hitchens fiercely believes that art can make things happen.

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Parkinson's disease

Downside up

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From The Economist print edition

MORTON KONDRACKE, an American political journalist, is a practised observer of the Washington scene. He lives there with his remarkable wife, Milly, who is dying of Parkinson's disease. To read "Saving Milly", his account of her struggle, is a harrowing experience, though not always in ways he intended.

Saving Milly: Love, Politics, and Parkinson's Disease
By Morton Kondracke

PublicAffairs; 300 pages; $25 and £17.99

Buy it at
Amazon.com
Amazon.co.uk

It is an honest but needlessly frank story of marriage, illness, anger and love, set against a battleground of fund-raising to find a cure. In some detail he describes his conversion from striving, successful media personality—a self-confessed rotter who wanted to marry someone grander than Milly and who was irked when she first fell ill—into a saintly spouse ungrudgingly tending to a failing wife.

Their story is in many places uplifting, and it would be inhuman not to want to sympathise. But with all confessional books of this kind there is a serious problem of tone and intent. Who wants to read about his "slow-dancing" Milly to the bathroom to change her "disposable underwear", or about her drooling, her gagging and their jokes about enemas?

Mr Kondracke's is not the only recent literary blossom from a newly heroic adult-nappy changer. In "Elegy for Iris", John Bayley, a literary critic and professor of English, similarly assaulted readers with the horrendous realities of looking after his wife, Iris Murdoch, a distinguished novelist, when, suffering from senile dementia, she could no longer look after herself. Need either writer have so encumbered us with the detail of their wives' bodily failures?

As to intent, Mr Kondracke's Milly was "a master of her universe", "a dynamo" who got him into Alcoholics Anonymous and off drink. Then, with illness, things change again. Soon, we read, he is completely at her beck and call, her champion. Is he now fulfilled or frightened to be indispensably on top, the hand that rocks the cradle? For a husband or wife to feel wrenching conflict when caring for a dying spouse is completely to be expected. Isn't such self-revelation best left in a diary to be read, if at all, after death?

This reviewer knows from experience that Parkinson's is a monster. Milly is particularly unlucky in having an unusually vicious form known as Parkinson-plus syndrome. It is swifter in its destruction of the central nervous system and responds poorly to symptomatic palliation. Milly is to be pitied. But the Kondrackes have many friends and even a prayer group on their case. She is fortunate, too, in having a feisty, stick-around husband, and the attention of two permanent carers.

Many Parkinson's sufferers will warm to this book's brave, upbeat approach. Yet, though the sections on politicking for more research money are unquestionably important, this reader did not find that "Saving Milly" held larger human lessons. Mr Kondracke calls his disease campaigning "God's work", and reports that God told him to "Take care of Milly". Heavy name-dropping—from the White House down through high places in Hollywood and back up to God—is both dazzling and sad. Mr Kondracke knows all these people and needs God too?

For plenty of us with it, Parkinson's is bad news all the way down. Despite the Kondrackes' valiant efforts, Milly continues to weaken and will soon die because there is no cure. So, to end on a less bitter note, if "Saving Milly" can prompt the giving of money for more Parkinson's research, then it will have been worth the effort of writing and reading—most of it.

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Stars of the past

Blowing on his cocoa

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From The Economist print edition

THE great troubadour from Hibbing, Minnesota turned 60 on May 24th. Bob Dylan's most recent album, "Time Out Of Mind", was widely hailed as his best in years—or is that decades?—and he picked up an Oscar earlier this year for his impeccably miserable song, "Things Have Changed". In addition to newspaper articles, radio retrospectives and TV tributes, two chunky biographies have appeared in the past few months: Clinton Heylin's "Bob Dylan: Behind the Shades" (William Morrow; Viking) and Howard Sounes's "Down the Highway: A Life of Bob Dylan" (Grove Press; Doubleday).

Positively 4th Street: The Lives and Times of Joan Baez, Bob Dylan, Mimi Baez Farina and Richard Farina
By David Hajdu

Farrar, Straus and Giroux; 336 pages; $25. Bloomsbury; £16.99

Buy it at
Amazon.com
Amazon.co.uk

Now, in "Positively 4th Street", David Hajdu revisits the folk music scene of the early 1960s to tell the intertwined stories of Mr Dylan, the sisters Joan and Mimi Baez, and Mimi's husband Richard Farina. Briefly, Ms Baez falls in love with Mr Dylan and uses her status as the reigning queen of folk to launch him on to the national stage—only to get a brusque Dear Joan from Mr Dylan when he moves up to full rock'n'roll stardom. Meanwhile, Mimi marries Richard Farina, a charismatic poet, writer, raconteur and musician, who promises her a life of wild adventure but dies four years later in a motorcycle crash.

The strongest stories in this book revolve around Mr Dylan, and these hardly overwhelm us with significance. The young singer, Mr Hajdu tells us, would sip black coffee while working in the morning before switching to red wine in the afternoon. Alternatively, he would sit on the floor of a studio apartment, surrounded by dozens of newspaper and magazine photos which (together with endless chain-smoked joints) inspired the disconnected phrases that gradually accumulated into such classic tracks as "Subterranean Homesick Blues" and "Mr Tambourine Man". And there are cameo appearances by Pete Seeger and Thomas Pynchon, among many others.

What's lacking is much insight into the broader meaning of the stories, anecdotes and events that "Positively 4th Street" recounts. If there is a larger point to Mr Hadju's ruminations, he keeps it to himself. Tellingly enough, *Vanity Fair* bought the serialisation rights; rather like a *Vanity Fair* article, the book, though capably executed, goes on too long, with too little payoff. This is cultural history told as celebrity soap opera.

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Cannes film festival

Welcome return

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From The Economist print edition

Italy is back, on movie screens at least

THIS year, the Palme d'Or belongs to the jury. After several festivals in which pretentious, mediocre movies have been honoured, the top Cannes film prize went to an aching account of bereavement: "La Stanza del Figlio" (The Son's Room), by Nanni Moretti.

Tall, bearded, self-assured but shy, with penetrating vulnerable eyes and the air of a man feeling his way in an unreliable world, Mr Moretti directed himself as an Ancona psychiatrist with a warm, close family stricken by the drowning of a teenage son. A little girl who knew the boy faintly eases their grief. Best known outside Italy for his episodic "Dear Diary" of 1993, he has never before reached so deeply into universal feelings. Mr Moretti's acceptance speech lamenting the election in his country of Silvio Berlusconi were greeted with warm applause.

The award marks a comeback both for Mr Moretti, after illness and his flimsy "Aprile" of 1998, and for Italy, which had two other notable films in the festival: Francesca Archibugi's "Domani" (Tomorrow) about the aftermath of an earthquake, and "Il Mestiere delle Armi" (The Profession of Arms) by Ermanno Olmi. Bedecked at first with subtitles in Latin, Mr Olmi's account of 16th-century Italian warfare baffled many, but impressed others with its clashes in the mist and its brutal surgery.

The Grand Prix went to "The Piano Teacher", by an unnerving Austrian director, Michael Haneke, who four years ago disoriented viewers with the unexplained, off-screen violence of "Funny Games". Isabelle Huppert was best actress, masochistically obsessed in the film with Benoit Magimel (best actor).

Best director was shared by David Lynch's "Mulholland Drive", a "Twin Peaks" lookalike, and Joel Cohen's monochrome "The Man Who Wasn't There" (or "All There"?), about a barber and a 1949 blackmail-murder. "No Man's Land", by a Bosnian-Belgian, Danis Tanovic, deserved its best-script prize. It traps a Serb, a Bosnian and a bomb between the lines. Neither a TV reporter (Katrin Cartledge) nor a UN colonel (Simon Callow) can help.

The newcomer's prize went to a magnificent Inuit film by Zacharias Kunuk, "Atanarjuat the Fast Runner". Despite the title it is three hours long. Yet those who watched to the end were transfixed. Snow crunches like gravel; oil lamps cast greasy light on igloo walls; men in furs lumber like astronauts; women scrape fish and seal meat with bone knives: the world of Inuit legend and Robert Flaherty is recreated unforgettably.

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R.K. Narayan

May 24th 2001
From The Economist print edition

Reuters

R.K. Narayan, an Indian storyteller, died on May 13th, aged 94

LIKE many young writers, R.K. Narayan found it difficult at first to get his work published. In 1934, after his novel “Swami and Friends” had been rejected by numerous publishers, he sent the manuscript to a friend in Britain who showed it to Graham Greene, a young writer who was doing rather better than Mr Narayan.

Greene opened the folder and read:

> It was Monday morning. Swaminathan was reluctant to open his eyes. He considered Monday specially unpleasant in the calendar. After the delicious freedom of Saturday and Sunday, it was difficult to get into the Monday mood of work and discipline...

Greene read on, and on. He was later to say that the book had something of the “beauty and sadness” of a story by Chekhov. He gently suggested some changes to the Indian’s English, and persuaded him to shorten his name from Rasipuram Krishnaswami Narayanaswami. This, Greene explained, would help “old ladies in libraries” to remember him. In those days libraries were the main buyers of books. Greene placed the book with Hamish Hamilton, an independent publisher interested in new writing (and now, like most former British independents, part of a conglomerate).

The two men, Greene and Narayan, corresponded for more than 50 years, until Greene’s death in 1991. Each time Mr Narayan completed a book he would send the manuscript to his friend and mentor who would cast a perfectionist’s eye over the text and offer a possible title. Greene would shout the praises of the latest effort to his famous literary friends, most of whom came to agree that Narayan was India’s finest writer in English.

It was only after 15 years of correspondence that Mr Narayan allowed himself the familiarity of addressing his friend as “Graham” instead of “Mr Greene”. The two men met only once in 1956, and then briefly, when Mr Narayan passed through London on his way to New York. Greene, although an enthusiastic traveller, seems not to have visited India, or if he did never lingered in the sleepy southern Indian towns that Mr Narayan depicted in Malgudi, the fictional community that is the setting for many of his novels. “Without him”, Greene said, “I could never have known what it is like to be Indian.”

America and India

For anyone, like Greene, seeking to understand India, R.K. Narayan is more accessible than Salman Rushdie and less cumbersome than Vikram Seth. In 15 novels and numerous short stories written in a spare style, and rarely more than 200 pages long, he illuminates the lives of small-town people. Gradually the reader comes to view the world through Indian rather than western eyes. After several visits to the United States, Mr Narayan sought to explain the difference:

> America's emphasis is on material acquisitions and a limitless pursuit of prosperity. The American works hard and earnestly and enjoys life. He has a robust indifference to eternity. The quality of life in India is different. In spite of all its deficiencies, irritations, lack of material comforts and amenities, and general confusion, Indian life builds up an inner strength. Indian philosophy lays stress on austerity and unencumbered, uncomplicated day-to-day living. From childhood an Indian is brought up on the notion that austerity and a contented life is good.

Mr Narayan's own upbringing was not austere. His father was a headmaster. The family had a pleasant house in Madras, and its members thought of themselves as modernisers. A brother, R.K. Laxman, became well-known as a cartoonist on the *Times of India*. Mr Narayan chose his own wife, although the custom was, and often still is, for an arranged marriage. All the same, he never rejected the "eternities" that colour Asian life. The day he began his first novel was selected for its auspicious quality by his grandmother, a devotee of horoscopes. When his wife died at an early age he sought to communicate with her through a medium. In "The English Teacher", his fourth novel, he describes the feelings of a man who has lost his wife: "Nothing else will worry or interest me in life hereafter." Mr Narayan never remarried and brought up their daughter Hema on his own.

His best work was still to come, notably "The Guide", a rags-to-riches-to-rags tale of a man who ends up contentedly as a spiritual adviser. If there is a moral in Mr Narayan's stories, it is in the need to "find" your real self. The book won many literary awards. Mr Narayan was often mentioned as a likely Nobel winner, but like Graham Greene never got beyond the shortlists. His fame spread, though. Greta Garbo once asked him to teach her the secrets of meditation. An embarrassed Mr Narayan said he had not been privy to them. The Indian government appointed him a member of the upper house of parliament in Delhi. In his first speech he spoke about children having so much homework they had no time to play.

R.K. Narayan never made the big money that famous authors are supposed to have. His books have been steady sellers rather than bestsellers. With the proceeds from a film of "The Guide" he bought what he said was his one indulgence, a Mercedes, coloured blue. "A calming colour," he said.

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Overview

May 24th 2001
From The Economist print edition

Europe's misfortunes continue. Year-on-year growth in **Germany**'s GDP plunged from 1.9% in the fourth quarter of 2000 to 1.6% in the first quarter of 2001—its lowest since the third quarter of 1999. German inflation jumped from 2.9% in April to 3.5% in May, the highest rate since December 1993. In **France** year-on-year growth in GDP fell from 2.9% to 2.7% between the fourth and first quarters. The **Netherlands** managed year-on-year growth of just 2.0% in the first quarter. The **euro** fell to a six-month low against the dollar.

Despite decelerating money growth, annual inflation in **Canada** is running at the highest rate since December 1991. Prices rose at an annual rate of 3.6% in the year to April, and by 0.7% in April alone. Canada's 12-month trade surplus swelled to $40.4 billion.

America's Dow Jones reached a record high for 2001 on May 21st. The stockmarket in **Australia** hit an all-time peak the next day.

Commodities

Timber prices in Chicago fell from 21-month highs after sales by Canadian mills eased shortages in America. Prices are still 50% higher than when the pact limiting duty-free shipments from Canada to America expired at the end of March. American producers have accused Canada of dumping. America's International Trade Commission has found evidence to support countervailing duties.

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Output, demand and jobs

May 24th 2001
From The Economist print edition

Output, demand and jobs

% change at annual rate

	GDP		The Economist poll GDP forecasts		Industrial production	Retail sales (volume)	Unemployment % rate	
	1 qtr	1 year	2001	2002	1 year	1 year	latest	year ago
Australia	− 2.2	+ 2.1 Q4	+ 2.1	+ 4.0	+ 3.1 Q4*	+ 3.0 Q1	6.8 Apr	6.6
Austria	+ 1.7	+ 2.6 Q4	+ 2.2	+ 2.5	+ 7.0 Feb*	+ 4.9 Jan	3.7 Mar	3.9
Belgium	+ 1.8	+ 2.4 Q1	+ 2.6	+ 2.6	+ 5.7 Mar*	− 2.8 Feb	10.2 Apr*	10.5
Britain	+ 1.4	+ 2.5 Q1	+ 2.3	+ 2.8	− 0.1 Mar	+ 5.9 Apr	5.1 Mar‡	5.8
Canada	+ 2.6	+ 4.0 Q4	+ 2.1	+ 3.2	+ 1.5 Feb	+ 3.5 Feb	7.0 Apr	6.8
Denmark	+ 4.9	+ 1.1 Q4	+ 1.9	+ 2.2	+ 5.2 Mar	− 0.6 Feb	5.4 Mar	5.3
France	+ 2.0	+ 2.7 Q1	+ 2.6	+ 2.7	+ 1.9 Mar	+ 1.9 Mar	8.7 Mar	10.0
Germany	+ 1.5	+ 1.6 Q1	+ 1.9	+ 2.5	+ 1.4 Mar	− 0.6 Mar	9.3 Apr	9.6
Italy	+ 2.8	+ 2.3 Q1	+ 2.2	+ 2.4	− 0.3 Mar	− 0.5 Feb	9.9 Jan	11.2
Japan	+ 3.0	+ 2.8 Q4	+ 0.6	+ 1.3	− 2.9 Mar	+ 2.1 Mar	4.7 Mar	4.8
Netherlands	+ 0.2	+ 2.0 Q1	+ 2.8	+ 2.9	+ 2.0 Mar	− 3.1 Feb	2.0 Apr§	2.7
Spain	+ 2.9	+ 3.7 Q4	+ 2.8	+ 3.1	− 3.7 Mar	na	13.5 Mar	14.8
Sweden	+ 2.4	+ 2.6 Q4	+ 2.6	+ 2.9	+ 6.2 Feb	+ 2.3 Mar	3.7 Apr*	4.7
Switzerland	+ 1.8	+ 2.5 Q4	+ 1.9	+ 2.2	+ 5.0 Q4*	− 0.6 Feb	1.7 Apr*	2.1
United States	+ 2.0	+ 2.7 Q1	+ 1.5	+ 3.0	− 1.0 Apr	+ 1.8 Mar	4.5 Apr	4.0
Euro area	+ 2.8	+ 3.0 Q4	+ 2.3	+ 2.6	+ 3.0 Mar	+ 1.2 Feb	8.4 Mar	9.2
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Finland	+ 3.0	+ 5.5 Q4	na	na	+ 7.0 Mar	+ 5.5 Feb	10.3 Apr*	11.0
Greece	na	+ 2.5 2000	na	na	+ 1.9 Dec	+11.8 Jan	na	na
Iceland	na	+ 4.4 1999	na	na	+ 4.2 1999	na	1.3 Jan	1.5
Ireland	na	+11.0 Q3	na	na	+38.6 Mar*	+ 4.0 Feb	3.6 Apr	4.3
Luxembourg	na	+ 8.5 2000	na	na	+ 0.2 Feb*	+ 9.4 Nov	2.6 Mar	2.7
New Zealand	+ 2.2	+ 1.6 Q4	na	na	+ 0.9 Q4*	+ 1.7 Q1	5.4 Q1	6.4
Norway	+ 0.2	+ 0.9 Q4	na	na	− 2.8 Mar	+ 0.8 Mar	3.7 Q1	3.9
Portugal	+ 2.2	+ 3.4 Q4	na	na	+ 6.0 Mar*	− 0.6 Feb	3.8 Q4	4.1

*Not seasonally adjusted. ‡Jan-Mar; claimant count rate 3.2% in April. §Feb-Apr.

Text refers only to the first 16 countries listed

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Prices and wages

May 24th 2001
From The Economist print edition

Prices and wages

% change at annual rate

	Consumer prices*			The Economist poll consumer prices forecast		Producer prices*			Wages/earnings		
	1 year		year ago	2001	2002	1 year		year ago	1 year		year ago
Australia	+ 6.0	Q1	+ 2.8	+ 3.6	+ 2.3	+ 5.2	Q1	+ 5.6	+ 5.6	Q1	+ 2.9
Austria	+ 2.9	Apr	+ 1.9	+ 1.8	+ 1.4	+ 2.9	Apr	+ 2.6	+ 2.5	Mar	+ 2.1
Belgium	+ 2.8	Apr	+ 2.0	+ 1.9	+ 1.7	+ 3.8	Mar	+ 8.6	+ 1.9	Q1	+ 3.3
Britain	+ 1.8	Apr	+ 3.0	+ 1.9	+ 2.3	+ 0.5	Apr	+ 2.3	+ 5.1	Mar	+ 5.7
Canada	+ 3.6	Apr	+ 2.1	+ 2.3	+ 2.1	+ 2.4	Mar	+ 5.8	− 0.9	Feb	+ 2.8
Denmark	+ 2.7	Apr	+ 3.1	+ 2.2	+ 2.2	+ 3.6	Apr	+ 5.7	+ 3.8	Q4	+ 4.1
France	+ 1.8	Apr	+ 1.3	+ 1.3	+ 1.4	+ 2.8	Mar	+ 4.5	+ 5.0	Q4	+ 3.4
Germany	+ 3.5	May	+ 1.4	+ 2.0	+ 1.4	+ 4.1	Apr	+ 4.4	+ 1.7	Mar*	+ 2.1
Italy	+ 3.1	Apr	+ 2.3	+ 2.4	+ 1.9	+ 4.1	Mar	+ 5.5	+ 2.0	Mar*	+ 2.1
Japan	− 0.4	Mar	− 0.5	− 0.4	− 0.3	+ 1.3	Apr	− 0.4	+ 0.5	Mar	+ 2.1
Netherlands	+ 4.9	Apr	+ 2.1	+ 3.9	+ 2.2	+ 5.1	Mar	+ 8.0	+ 2.9	Mar	+ 3.4
Spain	+ 4.0	Apr	+ 3.0	+ 3.1	+ 2.6	+ 3.2	Mar	+ 5.7	+ 2.2	Q4	+ 2.4
Sweden	+ 2.8	Apr	+ 1.1	+ 1.7	+ 1.7	+ 2.6	Mar	+ 4.1	+ 1.5	Feb*	+ 3.4
Switzerland	+ 1.2	Apr	+ 1.4	+ 1.2	+ 1.2	+ 0.9	Apr	+ 2.8	+ 0.2	1999	+ 0.7
United States	+ 3.3	Apr	+ 3.1	+ 2.9	+ 2.3	+ 3.7	Apr	+ 3.6	+ 4.3	Apr	+ 3.8
Euro area	+ 2.9	Apr	+ 1.9	+ 2.1	+ 1.6	+ 4.1	Mar	+ 4.9	+ 2.4	Q4	+ 2.3
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 3.0	Apr	+ 2.7	na	na	+ 3.0	Apr	+ 7.1	+ 4.3	Q4*	+ 3.5
Greece	+ 3.5	Apr	+ 2.6	na	na	+ 4.3	Mar	+ 7.9	na		na
Iceland	+ 5.5	May	+ 5.9	na	na	+ 4.2	April	+ 3.7	+ 9.2	Mar	+ 4.6
Ireland	+ 5.6	Apr	+ 4.9	na	na	+ 2.9	Apr	+ 5.4	+ 7.4	Q3*	+ 6.6
Luxembourg	+ 2.8	Apr	+ 2.7	na	na	+ 4.2	Feb	+ 2.0	+ 8.4	Oct*	+ 1.7
New Zealand	+ 3.1	Q1	+ 1.5	na	na	+10.2	Q4	+ 2.8	+ 1.8	Q1	+ 1.4
Norway	+ 3.8	Apr	+ 2.6	na	na	+ 9.8	Apr	+ 6.2	+ 4.3	Q4*	+ 4.0
Portugal	+ 4.5	Apr	+ 2.1	na	na	+ 4.7	Mar	+18.6	+ 2.2	Feb*	+ 2.8

*Not seasonally adjusted.

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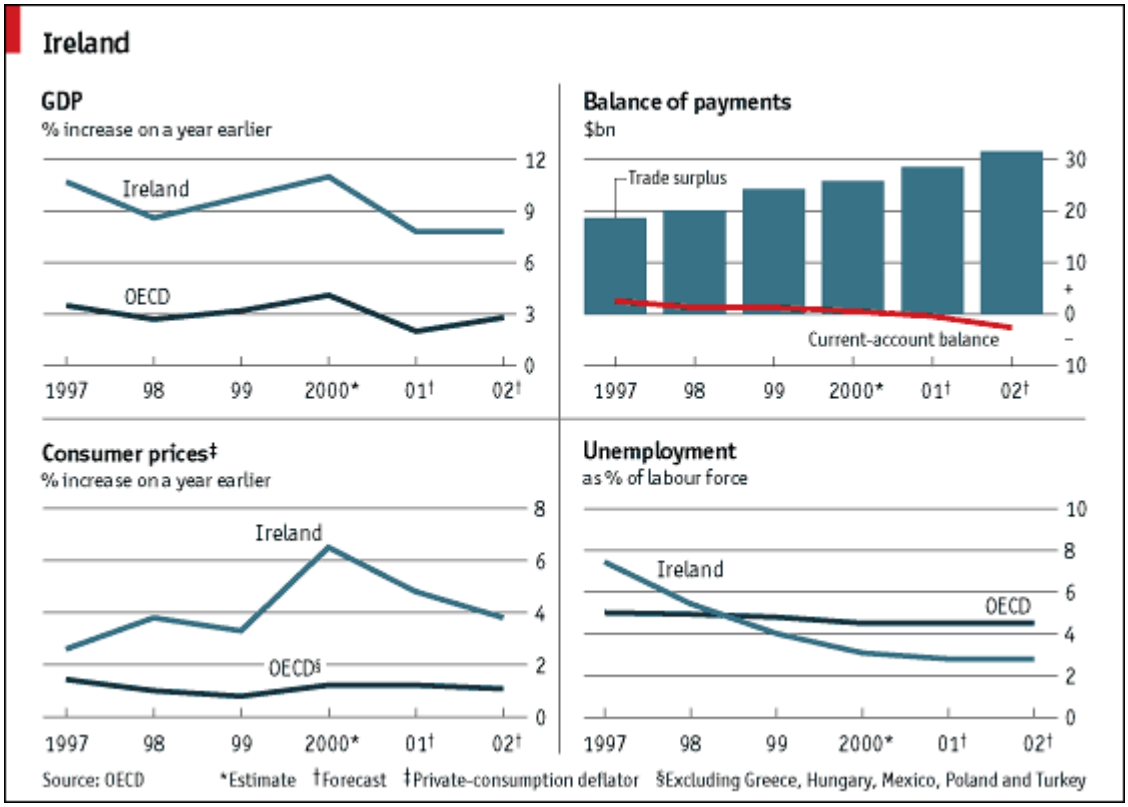
Ireland

May 24th 2001
From The Economist print edition

The Celtic tiger continues to roar, albeit at a more sustainable pitch. According to the OECD's latest country report, the Irish economy grew by a remarkable 11% in 2000. Cyclical strength in other industrial economies, strong demand for information and communication technology, and a weak euro all buoyed the emerald isle's fortunes. This year, the OECD reckons that Ireland's GDP growth will slow to less than 8%. That pace is close to the group's estimate for a sustainable rate of growth, but still almost four times the OECD's average. Exports are likely to contract this year, as OECD economies weaken and demand for information-technology products falls. Decreased exports will lead to a cut in business investment. The OECD predicts that the scarcity of labour will also reduce the scope for growth, as unemployment falls below 4%.



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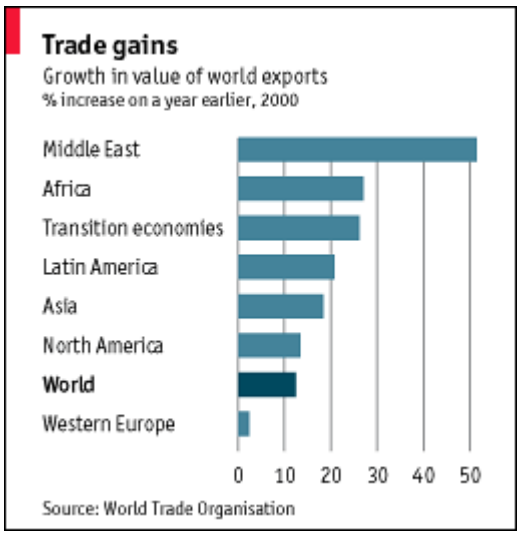
Trade gains

May 24th 2001
From The Economist print edition

The World Trade Organisation reports that the value of global trade rose by 12.5% in 2000. Slower growth is expected in 2001, thanks to the economic slowdown hitting rich countries.



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The Economist commodity price index

May 24th 2001
From The Economist print edition

The Economist commodity price index

1995=100

	May 15th	May 22nd*	% change on one month	% change on one year
Dollar index				
All items	71.5	71.7	+ 3.0	– 5.3
Food	68.6	68.0	+ 1.9	– 9.2
Industrials				
All	75.4	76.8	+ 4.3	– 0.1
Nfa†	74.8	76.7	+ 6.2	+ 6.7
Metals	75.8	76.9	+ 2.7	– 5.2
Sterling index				
All items	79.3	79.2	+ 3.6	– 2.0
Euro index				
All items	107.0	108.9	+ 6.2	– 0.7
Yen index				
All items	93.9	93.7	+ 3.4	+ 8.9
Gold				
$ per oz	267.35	282.85	+ 7.4	+ 3.1
West Texas Intermediate				
$ per barrel	28.84	29.42	+ 9.4	+ 1.6

* Provisional. † Non-food agriculturals.

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Stockmarkets

May 24th 2001
From The Economist print edition

Stockmarkets

Market indices

	May 23rd	2001 high	2001 low	% change on one week	% change on record high	% change on Dec 31st 2000 in local currency	% change on Dec 31st 2000 in $ terms
Australia (All Ordinaries)	3,362.0	3,370.7	3,094.3	+ 1.4	– 0.3	+ 6.6	– 0.4
Austria (ATX)	1,197.6	1,222.1	1,052.2	nil	–31.1	+11.6	+ 2.3
Belgium (Bel 20)	2,802.4	3,030.4	2,591.6	+ 0.7	–23.9	– 7.3	–15.0
Britain (FTSE 100)	5,897.4	6,334.5	5,314.8	+ 0.2	–14.9	– 5.2	– 9.6
Canada (Toronto Composite)	8,348.6	9,348.4	7,415.5	+ 2.5	–26.7	– 6.5	– 9.2
Denmark (Copenhagen SE)	913.1	1,002.1	818.3	+ 3.3	–12.1	+ 0.7	– 7.6
France (SBF 250)	3,613.8	3,820.2	3,107.9	+ 2.0	–17.7	– 4.2	–12.1
(CAC 40)	5,630.7	5,998.5	4,824.8	+ 2.0	–18.7	– 5.0	–12.9
Germany (Xetra DAX)	6,215.3	6,795.1	5,388.0	+ 1.1	–22.9	– 3.4	–11.4
Italy (BCI)	1,756.9	1,948.4	1,609.6	+ 1.3	–19.5	– 8.3	–15.9
Japan (Nikkei 225)	14,067.7	14,529.4	11,819.7	+ 2.7	–63.9	+ 2.0	– 3.3
(Topix)	1,375.2	1,441.0	1,162.0	+ 1.3	–52.3	+ 7.1	+ 1.5
Netherlands (AEX)	597.8	642.3	518.3	+ 2.0	–14.8	– 6.2	–14.0
Spain (Madrid SE)	924.2	963.9	818.6	+ 0.2	–19.4	+ 4.9	– 3.8
Sweden (Affarsvarlden Gen)	259.1	292.7	217.2	+ 5.3	–35.2	– 6.6	–16.0
Switzerland (Swiss Market)	7,699.4	8,135.4	6,574.0	+ 1.7	– 8.5	– 5.4	–13.6
United States (DJIA)	11,105.5	11,337.9	9,389.5	– 1.0	– 5.3	+ 3.0	+ 3.0
(S&P 500)	1,289.1	1,373.7	1,103.3	+ 0.3	–15.6	– 2.4	– 2.4
(Nasdaq Comp)	2,243.5	2,859.2	1,638.8	+ 3.6	–55.6	– 9.2	– 9.2
Europe (FTSE Eurotop 300) *	1,477.6	1,545.5	1,279.0	+ 2.2	–13.3	– 3.6	–11.7
Euro area (FTSE Ebloc 100) *	1,328.0	1,404.1	1,143.9	+ 1.7	–14.4	– 4.6	–12.5
World (MSCI) †	1,155.8§	1,249.2	1,014.6	+ 0.6	–20.2	na	– 5.4
World bond market (Salomon) ‡	427.8	447.8	427.1	– 0.4	– 7.0	na	– 3.7

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms. ‡Salomon Smith Barney World Government Bond Index, total return, in dollar terms. §Provisional.

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Trade, exchange rates and budgets

May 24th 2001
From The Economist print edition

Trade, exchange rates and budgets

	Trade balance*, $bn latest 12 months		Current account $bn latest 12 mths		The Economist poll % of GDP, forecast 2001	2002	Exchange rate trade-weighted† May 23rd	year ago	Currency units per $ May 23rd	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2001‡
Australia	− 2.7	Mar	− 15.1	Q4	− 2.9	− 3.2	72.8	75.5	1.93	1.75	2.74	1.66	1.60	0.1
Austria	− 4.6	Jan	− 4.2	Mar	− 2.5	− 2.0	99.7	99.8	16.0	15.2	22.8	13.8	13.3	-0.6
Belgium	+ 12.8	Mar	+ 11.6	Dec	+ 4.2	+ 4.3	98.1	98.4	46.9	44.5	66.7	40.3	38.9	0.7
Britain	− 44.3	Mar	− 24.5	Q4	− 2.1	− 2.0	107.6	105.8	0.70	0.68	–	0.60	0.58	1.2
Canada	+ 40.4	Mar	+ 12.7	Q4	+ 1.2	+ 1.0	78.0	78.9	1.55	1.51	2.20	1.33	1.28	2.6
Denmark	+ 5.9	Mar	+ 3.7	Mar	+ 1.4	+ 1.4	100.8	100.3	8.67	8.22	12.3	7.46	7.19	2.9
France	+ 0.9	Mar	+ 25.0	Feb	+ 1.6	+ 1.6	100.6	101.1	7.62	7.23	10.9	6.56	6.32	-0.5
Germany	+ 54.4	Mar	− 25.7	Mar	− 1.4	− 1.1	97.4	97.7	2.27	2.16	3.24	1.96	1.89	-1.7
Italy	+ 1.6	Feb	− 5.6	Feb	− 0.3	nil	71.8	72.1	2,249	2,134	3,204	1,936	1,867	-1.3
Japan	+ 98.9	Apr	+110.5	Mar	+ 2.2	+ 2.2	141.8	155.5	120	107	172	104	–	-6.3
Netherlands	+ 16.0	Feb	+ 13.7	Q4	+ 4.1	+ 4.0	96.9	97.2	2.56	2.43	3.65	2.20	2.12	1.3
Spain	− 39.5	Feb	− 16.9	Jan	− 2.9	− 2.6	73.6	73.8	193	183	275	166	160	nil
Sweden	+ 11.0	Mar	+ 5.5	Mar	+ 2.3	+ 2.2	76.5	83.5	10.49	9.19	14.9	9.03	8.71	3.6
Switzerland	− 0.4	Apr	+ 31.1	Q4	+11.8	+11.4	106.8	104.5	1.77	1.72	2.53	1.53	1.47	na
United States	−454.6	Mar	−434.9	Q4	− 4.3	− 4.0	119.8	112.3	–	–	1.42	0.86	0.83	2.1
Euro area	− 4.5	Mar	− 28.9	Feb	− 0.3	− 0.1	76.5	78.2	1.16	1.10	1.65	–	0.96	-0.6
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 13.3	Mar	+ 9.7	Mar	na	na	77.1	76.6	6.73	6.55	9.59	5.79	5.59	5.3
Greece	− 7.5	Q4	− 8.1	Dec	na	na	57.0	57.7	385	371	548	331	320	nil
Iceland	− 0.5	Mar	− 0.9	Q4	na	na	na	na	97.1	76.9	138	83.5	80.6	2.4
Ireland	+ 27.1	Feb	− 0.7	Q4	na	na	85.8	86.6	1.12	0.87	1.60	0.96	0.93	4.5
Luxembourg	− 2.4	Jan	+ 1.6	Q4	na	na	98.1	98.4	45.6	44.5	65.0	39.3	37.8	3.6
New Zealand	− 0.4	Mar	− 2.7	Q4	na	na	80.6	81.0	2.36	2.21	3.36	2.03	1.96	1.0
Norway	+ 27.5	Apr	+ 23.0	Feb	na	na	95.2	90.4	9.11	9.13	13.0	7.84	7.56	15.3
Portugal	− 12.4	Feb	− 10.2	Feb	na	na	88.6	88.8	227	221	323	195	188	-1.2

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100, Bank of England. ‡OECD estimate.

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Money and interest rates

May 24th 2001
From The Economist print edition

Money and interest rates

	Money supply* % change on year ago			Interest rates % p.a. (May 23rd 2001)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+14.1	+ 7.5	Mar	4.98	6.31	4.85	6.08	6.42	7.34
Britain	+ 7.7	+ 7.9	Apr	5.13	6.16	5.07	5.14	5.39	6.64
Canada	+11.4	+ 4.8	Apr	4.40	5.76	4.94	5.92	6.23	7.41
Denmark	– 2.2	– 6.5	Mar	4.90	4.58	4.89	5.35	5.66	7.21
Japan	+ 6.0	+ 2.7	Apr	0.02	0.03	0.01	1.29	1.68	0.58
Sweden	+ 5.8	– 0.3	Apr	3.99	3.95	4.60	5.34	5.17	5.52
Switzerland	– 2.2	+ 2.4	Apr	3.22	3.10	3.19	3.44	4.09	4.25
United States	– 0.1	+10.4	Apr	3.89	6.76	4.25	5.40	6.46	7.17
Euro area†	+ 2.1	+ 5.0	Mar	4.56	4.55	4.40	5.07	5.26	5.70

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 5.77%, Japan No.231 1.31%. Central bank rates: US fed funds 4.00%, ECB refinancing 4.50%, BOJ overnight call 0.01%, BOE repo 5.25%.
Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, OM Fixed Income Exchange, Warburg Dillon Read, WEFA Group, Westpac, Thomson Financial Datastream. Rates cannot be construed as banks' offers.

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Overview

May 24th 2001
From The Economist print edition

Taiwan's 12-month current-account surplus rose sharply in the first quarter, climbing by $2.5 billion to $12 billion.

Perhaps betraying contagion from Argentina's slowdown, **Chile**'s year-on-year GDP growth fell in the first quarter. **Colombia** also began to drag.

The stockmarket in **Mexico** rocketed by 12.4% over the week, as interest rates fell to seven-year lows.

Consumer-price inflation in **Singapore** edged up from 1.7% to 2.0% in the year to April, while **Hong Kong**'s deflation eased.

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Maternal mortality

May 24th 2001
From The Economist print edition

The World Health Organisation and UNICEF estimate that nearly 600,000 women die every year from complications associated with pregnancy and childbirth. The toll is greatest in poor countries such as the Central African Republic, where malnutrition, rampant disease and inadequate health care threaten both mother and child.

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Financial markets

May 24th 2001
From The Economist print edition

Financial markets

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	May 23rd		Dec 31st 2000	
	May 23rd	year ago	May 23rd	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	11.8	na	2,287.6	−0.3	+4.3	+4.3
Hong Kong	7.80	7.79	11.1	3.89	13,839.1	+3.8	−8.3	−8.3
India	47.0	44.2	66.9	7.75	3,674.5	+2.3	−7.5	−8.1
Indonesia	11,421	8,510	16,268	16.41	380.7	+1.2	−8.6	−22.5
Malaysia	3.80	3.80	5.41	3.30	560.8	−0.8	−17.5	−17.5
Philippines	50.4	43.0	71.7	10.56	1,446.2	−1.1	−3.2	−3.9
Singapore	1.80	1.74	2.57	2.29	1,687.0	+1.8	−12.4	−15.8
South Korea	1,287	1,133	1,832	5.83	622.6	+8.8	+23.4	+21.3
Taiwan	33.4	30.9	47.6	4.25	5,210.0	+2.5	+9.8	+8.8
Thailand	45.5	39.3	64.8	2.50	311.2	+3.6	+15.6	+10.3
Argentina	1.00	1.00	1.42	10.07	440.7	+2.6	+5.7	+5.5
Brazil	2.34	1.85	3.33	16.30	14,676.4	−0.3	−5.9	−21.6
Chile	606	526	863	3.40*	5,247.4	+0.6	+7.8	+2.0
Colombia	2,293	2,143	3,265	12.74	863.0	+0.2	+21.1	+18.1
Mexico	9.05	9.54	12.9	12.61	6,782.5	+12.4	+20.0	+27.4
Peru	3.59	3.51	5.1	9.72	1,318.7	+4.3	+9.1	+7.3
Venezuela	714	683	1,018	10.12	7,850.9	+1.7	+15.6	+13.2
Egypt	3.88	3.44	5.53	9.08	6,569.7	+0.3	−14.3	−14.0
Israel	4.13	4.21	5.89	5.20	426.4	+3.9	−13.8	−15.7
South Africa	7.94	7.10	11.3	10.71	9,465.4	+2.0	+13.7	+8.4
Turkey	1,115,750	619,980	1,589,274	59.00	12,052.4	−2.0	+27.7	−23.3
Czech Republic	39.8	40.1	56.7	5.04	428.7	+3.7	−10.4	−15.3
Hungary	298	286	425	11.15	6,948.6	+3.0	−11.5	−16.3
Poland	4.0	4.5	5.7	17.18	15,669.3	+5.5	−12.2	−9.2
Russia	29.1	28.3	41.5	25.00	207.9†	+8.2	+47.4	+45.1
EMF (MSCI)‡	1.00	1.00	1.42	na	337.0**	+4.3	na	+1.0
EMBI+§	1.00	1.00	1.42	na	212.0	+2.0	na	+5.0

*Inflation adjusted. †In dollar terms. ‡Emerging Markets Free. §J.P. Morgan Chase's Emerging Markets Bond Index Plus. **May 22nd.

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Economy

May 24th 2001
From The Economist print edition

Economy

	% change on year earlier						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 8.1	Q1	+11.5	Apr	+ 1.6	Apr	+22.3	Apr	+20.5	2000	178.0	Feb
Hong Kong	+ 6.8	Q4	– 0.2	Q4	– 1.4	Apr	–11.6	Mar	+ 8.8	Q4	115.1	Apr
India	+ 6.0	Q2	+ 1.3	Mar	+ 2.5	Mar	– 6.3	Mar	– 5.4	Q4	39.9	Apr
Indonesia	+ 4.0	Q1	+ 4.5	Q4‡	+10.5	Apr	+26.9	Mar	+ 5.5	Q3	22.3	Feb
Malaysia	+ 3.2	Q1	+ 0.5	Mar	+ 1.6	Apr	+15.3	Mar	+ 9.7	Q3	26.8	Mar
Philippines	+ 3.6	Q4	– 3.0	Feb	+ 6.7	Apr	+ 7.3	Mar	+ 9.4	Jan	12.2	Feb
Singapore	+ 4.5	Q1	+ 6.4	Mar	+ 2.0	Apr	+ 4.2	Apr	+21.8	Q1	80.2	Feb
South Korea	+ 3.7	Q1	+ 6.2	Mar	+ 5.3	Apr	+14.4	Apr	+12.8	Mar	93.5	Apr
Taiwan	+ 4.1	Q4	– 5.9	Apr	+ 0.3	Apr	+10.6	Apr	+12.0	Q1	110.6	Mar
Thailand	+ 3.1	Q4	– 1.8	Mar	+ 2.6	Apr	+ 3.7	Mar	+ 7.3	Mar	31.7	Mar
Argentina	– 2.0	Q4	+ 7.7	Apr	– 0.2	Apr	+ 1.5	Mar	– 9.4	Q4	21.9	Mar
Brazil	+ 3.8	Q1	+ 7.7	Mar	+ 7.1	Apr	– 1.4	Apr	–27.0	Mar	35.1	Feb
Chile	+ 3.3	Q1	– 1.7	Mar	+ 3.5	Apr	+ 1.5	Apr	– 1.0	Q4	14.5	Mar
Colombia	+ 1.8	Q1	+ 3.0	Mar	+ 8.0	Apr	+ 1.3	Feb	– 0.1	Q4	9.7	Apr
Mexico	+ 1.9	Q1	– 1.9	Mar	+ 7.1	Apr	– 9.0	Mar	–17.7	Q4	40.2	Mar
Peru	– 3.6	Mar	– 6.3	Mar	+ 2.7	Apr	– 0.4	Mar	– 1.7	Q4	8.2	Feb
Venezuela	+ 5.6	Q4	na		+12.1	Apr	+17.5	Nov	+13.4	Q4	12.0	Mar
Egypt	+ 6.5	2000†	+ 9.4	2000†	+ 2.4	Mar	–10.4	Q4	– 0.8	Q4	12.9	Jan
Israel	+ 3.0	Q4	+ 0.3	Feb	+ 1.2	Apr	– 7.5	Apr	– 0.7	Q3	23.5	Apr
South Africa	+ 3.3	Q4	+ 1.8	Mar	+ 6.5	Apr	+ 3.6	Mar	– 0.5	Q4	6.2	Mar
Turkey	+ 8.3	Q4	– 7.6	Mar	+48.3	Apr	–27.0	Feb	– 9.4	Feb	18.6	Mar
Czech Republic	+ 3.9	Q4	+ 9.8	Mar	+ 4.6	Apr	– 3.5	Mar	– 2.3	Q4	13.0	Apr
Hungary	+ 4.2	Q4	+ 5.3	Mar	+10.3	Apr	– 2.4	Mar	– 1.7	Mar	11.3	Apr
Poland	+ 2.4	Q4	+ 3.6	Apr	+ 6.6	Apr	–10.3	Mar	– 9.0	Mar	27.1	Mar
Russia	+ 6.8	Q4	+ 5.2	Apr	+25.0	Apr	+60.9	Mar	+46.4	Q4	25.9	Mar
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Pakistan	+ 3.9	1999†	+ 7.9	Oct	+ 4.2	Mar	– 1.7	Apr	– 2.5	1999	1.1	Jan
Saudi Arabia	– 0.8	1999	na		– 0.8	Feb	+24.9	1999	+ 0.4	1999	16.9	Mar

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Text refers only to the first 25 countries listed

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